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## PREFACE

THE preparation of a new edition of this work has afforded me an opportunity of undertaking a revision of certain portions of the text which the events of the last few years have rendered out of date. The study of Commerce as a branch of Applied Economics is of greater importance now than it has ever been, but the bewildering rapidity with which change occurs in commercial organisation imposes ever-increasing difficulties upon the student. Unless the student is provided with a definite scheme of study on logical lines, he will be unable to see the wood for the trees. He may accumulate a large mass of unco-ordinated knowledge which will be of little value because it is unsystematic. Hence, this work is an attempt to provide the student with a scientific study of the subject in the light of certain basic principles, and to illustrate the whole by reference to modern developments.

It is hoped that the work will continue to be of assistance to both teachers and students in connection with the examinations of such bodies as the Royal Society of Arts, the London Chamber of Commerce, the Lancashire and Cheshire Union of Institutes, the various Accountancy and Secretarial Associations, and also to University Classes in Applied Economics.

In the preparation of this work much help has naturally been derived from the researches of other writers, and especially from the valuable sources of information which are contained in the publications of His Majesty's Stationery Office. To all of these I am greatly indebted. My warmest thanks are also due to those friends who have in any way assisted me in my task, and especially to Mr. Noel Branton, M.Com., who has helped me throughout with the revision; Messrs. R. B. Scriven, A.I.C.S., and H. Branton for providing me with useful matter; and, finally, to my wife who rendered valuable assistance in the preparation of the MS. for the Press.

JAMES STEPHENSON

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## INTRODUCTION

THE partnership between science and industry since the Great War has created a period of technological development which is probably without precedent in the history of civilisation. As a result of improved technical methods and new knowledge, the volume of goods and services available for the use of mankind has increased manifold and, given favourable conditions, there is nothing to hinder an even greater expansion. As the Prince of Wales told the International Congress on Commercial Education held in London in 1932: "If all the employable labour were employed for a reasonable number of hours per week, the world would have at its disposal a volume of commodities and services that would enable the entire population to live on a higher level of comfort and well-being than has ever been contemplated in the rosiest dreams of the social reformer."

Unfortunately, however, industrial and commercial leaders have largely been content to limit the application of the scientific method to the workshop, and have too rarely associated it with the work of distribution. The result has been that we have been led to attempt the distribution of this enormous volume of new goods and services by means which are obsolete, with the natural consequence that the whole process has broken down. Worse than this, however, we find on every hand schemes of reform proposed by those who obviously have not taken the trouble to study carefully the complex questions involved. Moreover, many desirable reforms are being delayed because the exact knowledge necessary to effect them is not available. Thus, it has been stated that: "In spite of its great importance in the national economy, there is a regrettable lack of basic data as to the facts and technique of distribution. Information is required as to the number of establishments engaged in wholesale and retail distribution according to type and location, the main commodities dealt in, turnover, persons employed, stocks, operating expenses, equipment, credit practice, and so on. If ascertained at regular intervals it would enable the tendencies in the general distributive structure to be noted and assessed."<sup>1</sup>

<sup>1</sup> Report of the Reorganisation Commission for Fat Stock. Economic Series No. 39.



There is, therefore, a need, which is more urgent than ever, for the study of Commerce upon scientific lines. We are still obsessed with the idea that the creation of value is the same as the creation of material commodities, and on the basis of this fundamentally wrong assumption have perpetuated a whole series of injustices. The dismissal of Commerce as a "non-productive" activity, and the failure to realise its true importance, has rendered abortive progress in the sphere of technical production. It will be the aim of this work to show the nature and value of the services performed in the sphere of Commerce, and it will be seen that they are of equal importance with those performed within the factory walls. As the Final Report of the Committee on Education for Salesmanship stated: "Factories and workshops, warehouses and showrooms, and all personnel engaged in and about them, exist for the ultimate purpose of producing or distributing goods and services for sale. Such production is obviously in vain unless those goods and services can be marketed with profit to the producer and satisfaction to the consumer. The entire organisation of every business, from the directors' board room to the packer's counter and the delivery van, exists to serve that one end, and must be directed consciously and constantly towards it if the business is to prosper."

**MEANING OF SCIENCE.**—Whether the subject-matter of "Commerce" is to be called "science" or not, does not depend so much upon the subject-matter as upon the way in which it is studied; and it must be remembered that many unscientific things are done within the bounds of Physics, Astronomy, Chemistry, and other subjects. It is not the subject-matter which makes science, but the *method of study*. "The unity of all science," writes Karl Pearson in the *Grammar of Science*, "consists alone in its method, not in its material. The man who classifies facts of any kind whatever, who sees their mutual relation and describes their sequences, is applying the scientific method and is a man of science. The facts may belong to the past history of mankind, to the social statistics of our great cities, to the atmosphere of the most distant stars, to the digestive organs of a worm, or to the life of a scarcely visible bacillus. It is not facts themselves which make science, but the method by which they are dealt with." Some people imagine that because vagaries and speculations are put forward by men of science they necessarily are scientific; but whether they



are scientific or not depends upon the grounds by which they are supported, and not upon the men who put them forward.

In the first place, the man of science must not be prejudiced in any way. In a sense, however, this is impossible, for no one approaches any subject with an absolutely unprejudiced mind, for all knowledge is acquired by a process of apperception. This means that every new experience or new observation is at once assimilated by some knowledge which has already been acquired; consequently, the way in which the new phenomena will be observed depends on the kind of information with which the mind is stored. The mind seizes hold of new experiences, and moulds and interprets them according to the knowledge already possessed: so that to approach any new subject-matter with impartiality is impossible, since it will be coloured by the knowledge previously received. Moreover, the same object may appear different to different people, according to the knowledge they have already acquired.

It is therefore impossible to approach the subject-matter with a perfectly open mind, for some amount of prejudice or predisposition must be possessed by the persons studying the subject.

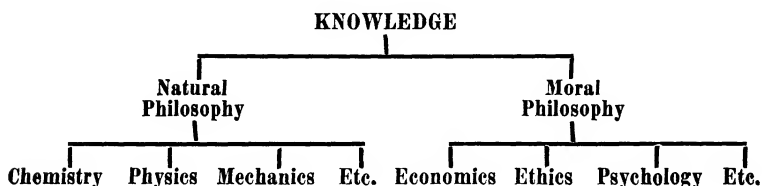
However, the scientist tries to see things not merely in their particularity or individuality, but in their *generality* or as types of a class—he tries to see the general principles involved. The man of science studies things not as individual objects, but as representatives of a whole class of things, and he endeavours to know, not the particular object, but the general laws or principles of that type.

Again, the knowledge which the scientist acquires is *systematic* and each object is studied as part of an objective system. This conception of system is one of the essential features of a scientific attitude. Things are regarded as being connected with other things, so that it is necessary to find out of what the connection consists.

**Abstraction.** In order to study things in a scientific spirit, it is necessary to abstract. It would be utterly hopeless to study the world of reality around us in its entirety. Until comparatively recent years, all branches of knowledge were regarded as belonging to one of two great divisions of philosophy—Natural and Moral. Human knowledge was supposed to have begun with



a homogeneous mass of human experience, which was gradually divided into natural philosophy and moral philosophy, and these were gradually differentiated into special sciences, each science being the systematic study of one group of things from a particular point of view. This may be represented as follows—



Each science is concerned with a different *aspect* of reality and is distinguished from every other, in that it studies not so much a different fragment of reality, but a different aspect. For instance, no science studies man in a totality, although human beings come under the scope of most sciences. In all the social sciences, man is the central subject of study. In Economics, he is studied from the point of view of his getting a living ; in Ethics, the aspect is that of right conduct ; whilst in Psychology, the aspect of study is that of mental experience. Thus, man is not studied in his entirety, but only from a particular aspect ; and this is known as *abstraction*. The advantage of thus concentrating one's attention on certain aspects is that it enables us to discover laws or uniform tendencies. But people are apt to confuse such tendencies with laws of Nature ; that is, they are apt to confuse what tends to be with what inevitably must be. This confusion was much encouraged by the triumph of modern physical science, which is largely the outcome of mechanical tendencies, such as the law of gravitation. The success obtained by physical scientists led students of social phenomena to follow in their train and thus formulate tendencies or laws ; but, in doing so, they often forgot that there are some very important respects in which the life of a human society differs totally from the movements of a merely mechanical system.

The laws regarding human society may be regarded as the apex of all scientific research, and for their comprehension the leading principles of more exact sciences and their relations one



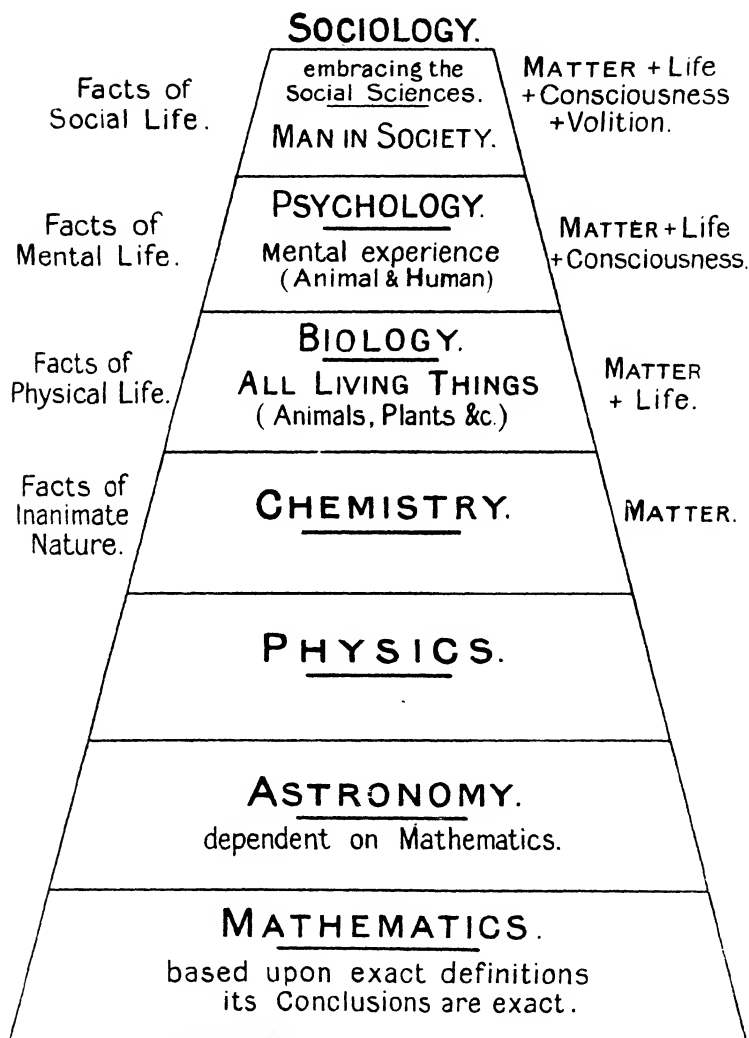
to another must be known. Social laws are merely statements of uniform action taken from experience, and differ from physical laws in the sense that the latter are permanent, whilst the former are subject to modification. Thus, social laws are the most complex of all scientific laws ; and this is due to the nature of the subject-matter of the social sciences as seen in the diagram on the next page.

The object of every science is to state, analyse, and explain the facts with which it is concerned. The study of Commerce, therefore, which is a study of human beings in society, must not be merely descriptive. The essence of every science is to give an answer to the question " Why ? " The student of Commerce must do his best to find the causes of the commercial phenomena which he records ; to show how and why they have come into existence. Thus, the aspirations of the commercial student should be the same as those of any other scientist, although his chances of success are not the same. There are often impediments in the way due to the nature of the facts. Commercial and Industrial phenomena are often so exceedingly complex, and the causes are often so hidden, that they can be detected only with the greatest difficulty.

In the following pages an attempt will be made to describe and illustrate the working of economic principles in the sphere of modern commerce. " The theory of economics does not furnish a body of settled conclusions immediately applicable to policy, but is rather a technique of thinking which enables its possessor to draw reasonably accurate conclusions." Modern commercial organisation grows increasingly complex, and he who would understand its structure and attempt to cope with its problems must equip himself for the study by acquiring this technique. The study of economic theory must therefore not be regarded as an end in itself, but merely as an essential preliminary to a study of economic institutions as they actually exist. The aim of this work will be to show this application of theory to practice, by dealing in broad outline with modern commerce, paying special attention to current developments and tendencies. On account of the wide nature of the subject, and the large amount of ground which has to be covered, it is impossible to deal with any portion of the subject-matter in detail. Much must be left to the initiative of the student.



**ARRANGEMENT OF THE SCIENCES**  
(According to exactness of Subject-matter)





# PRINCIPLES AND PRACTICE OF COMMERCE

## SECTION I—GENERAL PRINCIPLES

### CHAPTER I

#### THE STUDY OF ECONOMICS

**ECONOMICS.**—The basis of commerce as a subject of study is economics. This is the science which deals with human conduct in relation to wealth. It is concerned with the actions of men when they are engaged in producing, exchanging, sharing and consuming those things which are collectively known as wealth. Thus, according to Professor Marshall: "Economics is the study of mankind in his ordinary business of life"; or, as Dr. Spencer puts it: "The study of mankind when he is getting a living." Since economics is the study of the production, distribution, exchange and consumption of wealth, the question arises as to what is wealth.

**WEALTH.**—The idea expressed by this word "wealth" has changed considerably from its original meaning. If the term be traced to its Anglo-Saxon meaning it is found to indicate the state of being well, in the same way as the word "health" means the state of being "hale." Again "dearth" was the state of being dear. In the book of Common Prayer the word appears in "Grant him health and wealth, long to live . . ." Here the word "wealth" has reference, not to affluence, but to a state of well-being. From its close connection with "weal" or the state of being well, it occurred to men that it was impossible to be particularly well without something to eat, something to wear, and somewhere to sleep. Hence the word "wealth" was applied to those things by which man is kept alive.

Next there was a time when the instrument which transferred the ownership of those things which contributed to health, viz., money, came to be regarded as wealth in a peculiar sense. Throughout



the sixteenth and seventeenth centuries money was the wealth *in excelsis*. Of course, even the Mercantilists, aided by their great leader, Thomas Mun, whose book *England's Treasure by Foreign Trade* was published in the seventeenth century, knew quite well that money was not the only kind of wealth, but they did teach that riches in the economic sense consisted entirely of things exchangeable for money. So up to that time wealth consisted exclusively of things that possessed an exchange value.

According to John Stuart Mill, material things are certainly wealth ; but can anything immaterial be included in the conception of wealth ? It was one of the unfortunate and unhappy results of Mill's fatal distinction between productive and unproductive labour that led him to exclude from the concept of wealth any utility such as services. A labourer's skill was not wealth unless it was of a kind which was exerted in the production of a material object. According to this view, the skill of the bricklayer is wealth, whilst the skill of the architect is not. The fallacy of this argument has long since been exposed. Happily, what is called " Direct Services " is included by practically all modern economists.

**MODERN MEANING OF WEALTH.**—The qualities which are considered as involved in the word " wealth " by modern economists are generally stated to be three in number. For a thing to be economic wealth it must be—

- (1) Transferable ;
- (2) Limited in Supply ;
- (3) Useful, in the sense of procuring a pleasure or preventing a pain.

A thing cannot be wealth unless it satisfies a human want. Again, a thing which satisfies a human want will at any rate be a " good " but it will not necessarily be economic wealth, unless it is a " good " produced as a result of human effort. If nature supplies the thing free, it cannot be regarded as economic wealth, although it may be counted as a " good." For a thing to be wealth it must be limited in supply in the sense that it has to be worked for, and it must be useful in the sense that it will procure a pleasure or prevent a pain.

Further, among the things which are procured in return for labour are certain " rights " to wealth. The holder of a bill of exchange can demand payment on the date of its maturity, so that it represents a right to wealth. But although rights form part of



individual wealth, they cannot form part of the national wealth because whatever rights are added to one individual must be subtracted from another. Hence there is a national wealth in which individual rights do not count. According to Professor Marshall, a good many of the free gifts of nature come under the heading of national wealth. For instance, he would classify the River Thames as part of the wealth of England. This is probably going too far, for no one has made the Thames River. The Thames Embankment has been made, but not the Thames itself, and therefore the latter can scarcely be classed among the economic wealth of England.

An individual may be regarded as well-to-do when he has many wants, and the wealth to satisfy them. Indeed, he is in a state of well-being or civilisation when he wants many things and gets them, so that the existence of wealth depends upon the pre-existence of the human want ; and it is this fact which makes economics one of the psychological sciences, i.e., a science of the human mind. Human wants become motives to action. A person desires a certain thing, and that inspires his actions with a view to acquiring the particular object. These motives can be measured against one another by means of exchange, and this is the great advantage which economics possesses over the other social sciences. In psychology, which treats of the emotions, it may be said that a person hates, but the extent of that hatred cannot be measured. In economics, however, if a person is able and willing to give 2s. 6d. for a certain commodity and 2s. for another, these motives may be measured as being in the ratio of 5 : 4. But although motives can be measured by means of money, it must be noticed that it is only a rough estimate. The expenditure of 2s. 6d. by one man does not necessarily indicate the same motive as 2s. 6d. spent by another person. Again 2s. 6d. spent by a certain person to-day may be quite different from the expenditure of the same amount twenty years hence. The economist relies on the doctrine of averages. Although the individuals may alter, the group tends to remain the same. For this reason it can be said that if a commodity is sold for 2s. 6d., then on the average it represents the desires of that community to possess the commodity. It may be that the sacrifice of 2s. 6d. is practically negligible to a rich man and very great to a poor one, but taking the group an average may be struck showing that 2s. 6d. does



represent a certain intensity of desire. An economist, however, has neither to classify nor censure desires—he has merely to measure them.

The study of economics is usually divided into the Production, Exchange, Distribution, and Consumption of Wealth, although the order of treatment varies with different writers.

**PRODUCTION.**—This branch of the study is an inquiry into the means by which natural resources are so altered as to cause them to be desired by men. It is the study of the re-arrangement of pre-existing matter from a form in which it is less, to a form in which it is more capable of satisfying human wants. In short, it is the re-arrangement of the environment of which the human body forms a part. For example, a table may be regarded as a re-arranged tree. Again, in learning to ride a bicycle, the human body must be so arranged as to get the nerve centres in a position which will afford confidence to the rider. Hence the acquirement of skill is a product of personal labour, so that personal wealth can be produced. Increase of effort will give increase of results to a different extent according to the direction in which the effort is employed. Increase of effort employed to make clothing in a factory, will give more than a proportionate increase of clothing, whilst an increase of effort in a field will tend to give less than a proportionate increase of return. These facts are summed up in the two fundamental laws of economics—the laws of increasing and of diminishing returns. (See page 24.) A curious fact about these two laws is that diminishing return does not begin to operate in a business immediately, whilst increasing return ceases to operate in the end. Take, for instance, what Professor Marshall calls a Representative Firm with average ability, and ordinary access to internal and external economies. Such a firm may be likened to a forest tree. It may gradually increase until it becomes the largest in the forest, and then gradually fade away whilst others take its place. In the same way, there is a limit to the economic or profitable size of a firm. It may continue to grow and at the same time become more and more productive, but finally it becomes too unwieldy so that smaller and more efficient firms take its place.

**EXCHANGE.**—For a study of this subject it is necessary to inquire into the mechanism by which wealth is enabled to pass from hand to hand. The main function of exchange is to increase the utility



of commodities by transferring them from places where they are required less to places where they are required more. The system of exchange is the result of the gradual development of the division of labour in the industrial organism. In the beginning, goods were transferred by the owner direct to the consumer without the intervention of any medium. Next there evolves the market within which exchanges are effected. With the increase in the variety of the goods brought to be exchanged, and the necessity of having more exact information concerning the market conditions, there develops the trader who has rendered the exchange of goods into a specialised calling. The exchange of goods increases with the progress of economic development, with the extension of division of labour, and with the growth of production. The perfection of transport facilities and the system of banking enables exchanges to be effected more speedily and methodically.

**DISTRIBUTION.**—This section of economic study inquires into the manner in which the total wealth produced by the community is divided among the various classes of claimants for a share in it. These may be classified as follows—

- (1) The State's share, in the form of Taxes ;
- (2) The Landowner's share—called Rent ;
- (3) The Capitalist's share—called Interest ;
- (4) The Labourer's share—called Wages ;
- (5) The Organiser's share—called Salary ;
- (6) The Entrepreneur's share—called Profits.

Thus, in the modern economic organisation, there is in the process of production a combination of persons ; such as the entrepreneur, landowner, capitalist, and labourer, each of whom demands his share of the product, not through any power of authority, but claims it on the ground of his economic participation in production. Distribution, therefore, resolves itself into a form of strife, the result of which is determined by the conditions of the market. It is, however, influenced to a certain extent by the customs, morals, and legal institutions prevailing in the community. The magnitude of the total net production of the country is a determining factor in the sharing of the wealth which is to go to any single factor. This net output of the total economic activities of a people is known as the **national dividend**.

The aim in a competitive system of society is to distribute the



national dividend in such a manner as to correspond to the actual services rendered by each factor which has contributed to its production. Thus, if the total wealth earned by the community be so divided, each recipient should contribute an equivalent service for the amount he receives as measured by market forces.

**CONSUMPTION.**—This is the section of economics which inquires into the ultimate result of all that is produced. It is concerned with the removal of the utility of a commodity, by the satisfaction of the want for which the commodity was produced. Consumption is the aim and end of productive activity. Its far-reaching effects on the entire conditions of human life render its study of great economic significance. In the case of material commodities, consumption terminates with the complete removal of their former utility, and in the case of personal services, simultaneously with their effect on the consumer.

The satisfaction of human want is attained *indirectly* if the commodity is used in the production or manufacture of another commodity, and *directly* when it takes place with the object of satisfying an immediate human desire.

### TEST PAPER I

1. Explain the meaning of the term "Science."
2. What is the function of "abstraction" in scientific study?
3. Describe the changes in meaning through which the term "wealth" has passed.
4. According to modern economists, what attributes must be possessed by a commodity in order to be classed as "wealth"?
5. What do you regard as the chief characteristics of wealth? Consider whether the following should be included in wealth, assigning your reasons in each case: canals, rivers, honesty, business connection, cannon.
6. Discuss the definition of Economics as "The science of social action which is dependent upon measurable motives."
7. If Economics be defined as the social science which deals with action resulting from measurable motives, explain exactly what may be taken as the standard of measurement.
8. Economics has been shortly described as "a study of the methods in which men use their efforts for the satisfaction of their wants." Explain and develop this account.
9. Examine carefully the meaning of the term "Production" as used in Economics.
10. *Production* consists in the creation of *values*. Man does not create objects—only *utilities*. Explain and comment on these propositions defining the terms in italics.
11. In what manner is the total wealth produced by the community divided among the various claimants for a share in it?
12. What in your opinion is the aim and end of Productive Activity?



## CHAPTER II

### THE RELATION OF ECONOMICS TO OTHER SUBJECTS

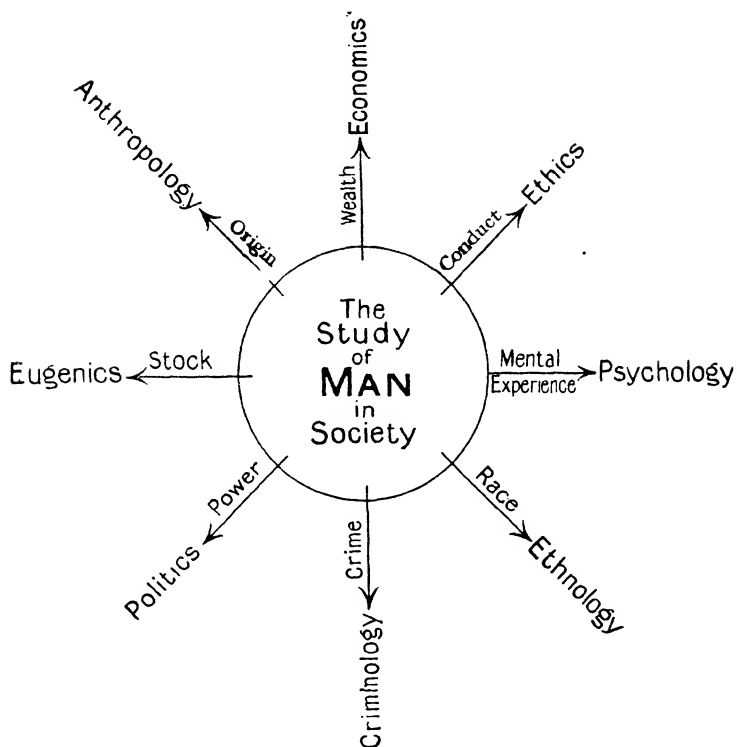
ECONOMICS, like every other science, is related to other departments of knowledge. (See Diagram, page 8.) In every science regard must be had to the researches made in other subjects. Each science has to trespass on the preserves of other sciences, but many things have to be taken for granted. Except in metaphysics, the student is not concerned with first principles, and then only in dealing with philosophy. Science may be regarded as an elaborated common sense which takes a great many things for granted, for if it did not do so, no intellectual progress would be made.

Economics may be regarded as one relatively independent division of the general philosophy of society, or, in other words, as a branch of Sociology. Other sciences of the same level would be jurisprudence, politics, the study of comparative religion, psychology, and, generally, the study of other branches of social science. Each branch must have its own specialists. Economics investigates the activities of man in relation to wealth. The study of the phenomena of wealth, however, cannot be completed without taking into account the influence of other social facts. The best results can be obtained only by bringing together the economic conclusions arrived at in the light of the knowledge amassed in the other branches of scientific investigation. In this way, alone, is complete knowledge possible. On the one hand we must specialize, on the other hand we must take into consideration other branches of social phenomena in establishing the truths discovered in our own subject.

**RELATION TO PHYSICS.**—The economist is obviously concerned with problems which are related to wealth. It is not his business to act as a physicist. To-day, physics has reference to applied mathematics, mechanics and heat, but in the old sense it was applied to the study of nature. It is applied to those sciences which deal with material things, and would include agriculture. It is the duty of the economist to take into account the various physical laws which affect agriculture. He must take into account such laws as those of diminishing and increasing returns in so far as they influence the social aspect, and he must understand the



## RELATION OF THE SOCIAL SCIENCES



Sociology is the study of man from every aspect, and therefore embodies the principles of all the social sciences.



operation of other physical laws to the extent that they will help him in his economic investigations. For instance, in discussing the question of Free Trade or Protection, the physical peculiarities of different countries, such as soil and climate, must be taken into account, but the economist need not make himself responsible for the correct exposition of these physical differences. He takes them for granted, as soon as some other scientific department has accepted them.

Modern sciences have been based largely on physics or physical analysis, but that has not always been the case. In the seventeenth century the only science which people could respect was mathematics, and the mathematical method became the method for all other sciences. The peculiarity of mathematics is the inter-connection between facts which are given in the abstract and from which results can be built up. In physics, the student has to deal, not with facts given in the abstract, but with events and with material bodies between which it is assumed there is a strict inter-connection from the point of view of causal relationship. In short, modern physical science assumes that all the phenomena of nature are inter-connected, and, moreover are inter-connected in uniform ways.

**RELATION TO PSYCHOLOGY.**—In dealing with the relation of economics to physics, it has been seen that the economist has to take into account the results obtained by the physicist but has not necessarily to become a physicist himself. In the same way the economist has to borrow from psychology, which is concerned with the processes of the mind or mental experiences, and the connection here is probably more intimate than in the case of physics.

It is obvious that the economist must never forget the fact that he is dealing with the human mind. He is not dealing with mechanical machines which will act in a certain way. It is the science of psychology which tries to discover the uniform ways in which the human mind operates. The economist must not ignore the laws which permit of economic relationships resulting from the psychological operations of the mind ; he must borrow them from the psychologist.

Economic laws or tendencies are different from the psychological laws. Psychological laws are simply laws of human nature, whereas economic laws are complex social facts which are rather determined



by the simple laws of human nature, so that these simple psychological laws of human nature must be taken into account in investigating the complex facts of society. Thus, for instance, the economist does not attempt to analyse the feelings of self-interest, but regards these feelings as facts which he does not attempt to explain. Again, man's desire for a greater gain in preference to a smaller one, and his willingness to undergo a present loss for a future gain, are psychological facts which the economist takes for granted. Certain psychological facts must be taken into account in the study of economics. Take, for instance, the saving of money. People may save money simply because it has become habit, so that their saving is not the outcome of purely economic factors, but of purely psychological factors. Again, dealing with the supply of labour, it would be a mistake to imagine that all values are determined by purely economic forces. If that assumption is made, certain facts will be inexplicable, as, for instance, where people undertake all kinds of work without any economic return at all. Again, some people continue to work hard although they have no need to do so, whilst others may do an enormous amount of work as the outcome of purely religious motives. These are psychological facts which must be taken into account. Further, there is sometimes a tendency to speak of the mobility of labour, as though it were determined entirely by economic forces, but that is not true. The mobility of labour is hampered by friction or inertia ; people may know that they can do better in some other place, but they have not the enterprise to remove away to get that additional advantage. The assumption made in economics that labour will move from industry to industry, and from one part of the country to another sufficiently easily, and in sufficient amounts to secure an approximation to equal remuneration for equal effort of a certain type, is therefore incorrect, since it is modified by the influence of custom, ignorance, dislike of change, etc.

Strikes are sometimes prolonged by doggedness which is unprincipled, and in trying to account for financial crises there is often a non-economic factor at work which cannot be explained on economic grounds. There are many people who are easily frightened out of their wits, and on the rumour that a certain financial house is unsound, they will rush to withdraw their capital. Their own stupidity may bring about disaster. The economist has to



pay regard to the results of psychology, but he need not be a psychologist himself ; he can take over the facts in trust from the psychologist.

**RELATION TO ETHICS.**—There was a time when the economist was eager to defend the relationship of economics to ethics. The invention by writers of the middle of the nineteenth century of an imaginary being whose sole motives and incentives to action—such as self-interest and the desire to obtain the greatest possible gain with the least possible effort, etc.—were economic, led people to regard economics as the dismal science. These peculiar notions of the character of the economic man led to a reaction in which Carlyle and Ruskin made their voices heard, and of late there has been a distinct demand for a reconsideration of the bearing of economics and ethics.

The subject-matter of ethics is human conduct specially regarded from the point of view of being right or wrong ; the study of the conduct of man to man. This can be studied in three different ways—

(1) Human conduct may be studied from the point of view of development, that is, from the historical point of view. In this case the history of the development of human conduct is traced, and the actual facts at different stages of human development are described without examining whether the conduct is right or wrong. An inquiry is made into the behaviour of early races towards each other, and an attempt is made to show the connection between the earlier conduct and that of to-day. Thus, among the aborigines in some parts of Australia it is considered right that an aged mother should be killed. On comparison it is seen that this is not the ideal of modern Europe.

(2) People's ideas with regard to conduct may be studied. For example, some people believe they should conduct themselves differently on Sundays from the week-days. Generally speaking, there is an intimacy between people's ideas of conduct and conduct itself.

(3) Apart from the historical development of conduct, an inquiry may be made into the question as to what ought to be the right standard of conduct. The investigation then is one of ideals and not of facts. What should be the ultimate aim of man's conduct so as to enable him to live in the best possible way ? This was a



subject of inquiry as early as human consciousness became reflective and speculative.\*

These three lines of inquiry are intimately connected, and the ordinary student will consult the wisdom of the past ages in order that he may better understand modern ideals.

In economics, then, each of the above lines of inquiry must be taken into consideration, but more especially the ideas of conduct which at present influence the minds of the people and help to determine their behaviour.

The relation between economics and ethics is, that the former is concerned with *means*, whereas the latter is more concerned with the *ends* to be achieved. Clearly it is unwise to study economic means without reference to the ends aimed at. One source of danger is to regard the means as an end in themselves. For instance, there is a tendency to regard the mere increase of material commodities as a social end. It is necessary ever to keep in view the end of human endeavour and to remember that the ends considered in economics are not ends in themselves but merely means. Anything in the nature of an adequate study of society should include a careful consideration of the ends of human conduct, as well as the means which might promote the attainment of such ends.

**RELATION TO POLITICS.**—The older designation of economics, viz., political economy, is rather a misleading one; it suggests a relationship between economics and politics which really does not exist. The fact is that the older conception—political economy—was used in the same sense as the word *Social*, and economics is a social science. The Greek word *Poly* means a "city" or "State," and political economy had reference to the social life of the State; but at the present day the word "political" has reference, not to the social side of life, but to the governmental side of life, and politics is the study of the different forms of government.

The older title of political economy is misleading to the extent that it suggests a more intimate relationship between economics and politics than really exists. If a discrimination is to be made between social and political, it would be better to say that economics is rather a social than a political science. There is some connection between the science of economics and politics; for economics



has to take into account conditions of government and law. But still, economics is primarily concerned with man in his social relationships, as distinct from man in his political relationships, and it is only in certain departments of economics that man is considered as a member of the State government.

While economic doctrines may be relative to particular political conditions, they are more frequently dependent upon different stages of industrial organisation ; and on the whole it would be rather incorrect to say there is absolutely no connection between the stages of social development and the different stages or types of government. Herbert Spencer shows a certain tendency towards democratic forms of government in certain types of industrial organisation. There is, however, insufficient connection between the different forms of industrial organisation and different modes of government to necessitate any special attention being given to the particular kinds of government in dealing with such problems as those of distribution and exchange, for they are more connected with different forms of industrial organisation.

In the case of applied economics, however, there is a much more intimate connection with economics than there is between pure economics and politics, so that problems of this kind assume a certain kind of government. Applied economics is concerned with the economic activities of the State in its corporate capacity.

## TEST PAPER II

1. Is it necessary for the economist to take physical laws into consideration when carrying out his investigations ?

2. Show in what way psychological facts must be taken into account in the study of Economics.

3. Explain the relation of Economics to Ethics.

4. Discuss the statement that the economist is primarily concerned with " what is," not with " what ought to be."

5. Explain clearly the scope of " Politics," and specially consider its relation to Economics.

6. In what respect was the older title of " Political Economy " misleading ?

7. Describe generally the relation existing between Economics and other social sciences.

8. Is Economics a science ? Whether your answer be negative or affirmative, make clear the meaning which you think properly belongs to the word " Science," and compare the nature of Economics with that of other academic disciplines.

9. What are the proper limits, if any, of the science of Economics ? In what way is it related to Sociology ?

10. What is meant by looking at a question (a) from an economic, and (b) from an ethical point of view ?



## CHAPTER III

### THE ECONOMIC BASIS OF COMMERCE

JUST as economics is part of the study of sociology, so commerce is a section of economic study. Economics deals with man in his endeavour to earn a living, and embraces all persons engaged in the production of wealth; whilst commerce is concerned with a *fraction* only of such persons. It includes only those who are engaged in the production of values by the transference of commodities from the place of origin or of manufacture to that of consumption. Commerce is, therefore, chiefly based upon that department of economics known as "Exchange," and in part upon "Production."

**CHIEF REASONS FOR COMMERCIAL INTERCOURSE.**—Commerce signifies the exchange of all reciprocal goods and services, and includes the whole of the labour engaged in rendering, as intermediaries, economic services of any kind.

It has naturally passed through many stages of development, till it now forms a most important part of the economic organisation. There are three main causes which have led to the rise and continuance of a system of commercial intercourse—

1. **The diversity of natural resources** and their geographical distribution over the surface of the earth.

2. **The differences of human want.**

3. **Division of Labour**, which is a consequence of the above two factors.

The diversity in the geographical distribution of wealth renders it necessary for man to obtain from distant areas those commodities which cannot be produced within his own locality. Hence, there are established extensive commercial relations between the various natural zones, such as the intercourse between lands with temperate, and those with tropical or sub-tropical, climates.

The differences of mankind, that is, of races and peoples, help to account for an extensive system of exchange between the inhabitants of different nations, between peoples of different modes of living, and between new and older countries of higher and lower civilisations.



Finally, division of labour, in consequence of its great advantages, soon asserted itself, and gave rise especially to the exchange of masses of goods between different trades and industries, and between town and country districts.

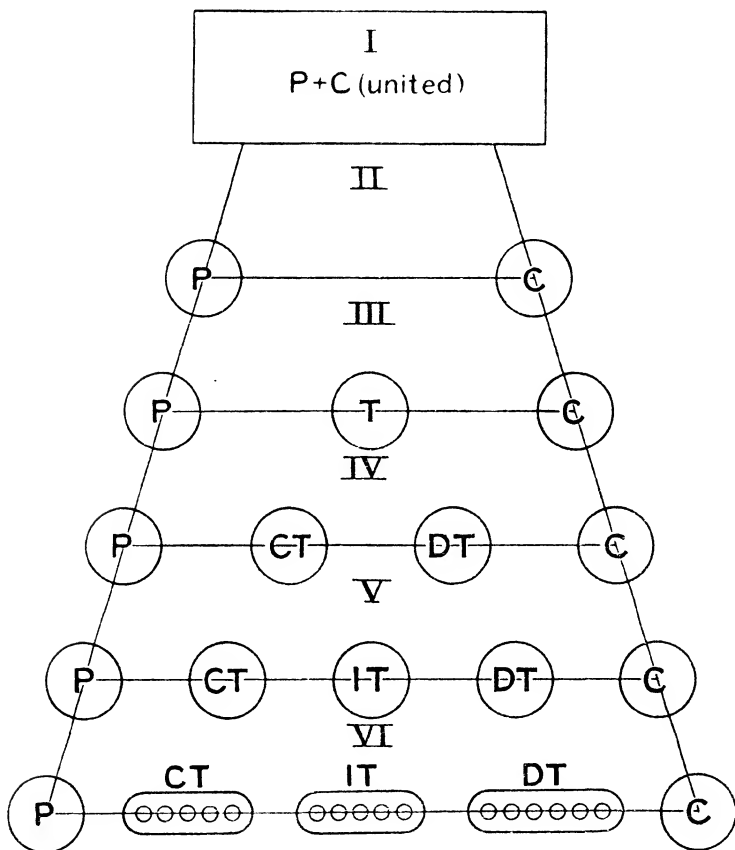
Throughout the whole history of commerce, the influence of these three factors is constantly in evidence, and their effects are clearly seen in the various stages of commercial development from the lowest forms to that now in existence amongst the most progressive peoples. The *forms* of commerce may be regarded as the best indication of the economic condition of a country. The most usual classification distinguishes, in the first place, a lowest stage of accidental intercourse between neighbours, in which exchange of a very primitive form takes place occasionally, and in which the custom is for all the processes of production to be effected within the family group. This stage, together with succeeding stages of development, is shown in the diagram on the next page.

**STAGES OF COMMERCIAL DEVELOPMENT.**—In this **first stage** of economic development, division of labour scarcely exists, being limited to the members of the family. Under these circumstances, man is engaged chiefly in hunting, fishing, the making of arrows, the production of weapons, the skinning of animals, etc.; whilst his wife and daughters devote their time to the building of huts, the gathering of herbs and fruits, the cultivation of the fields, the grinding of corn, and similar work. Man only gradually took upon himself the more difficult tasks, such as house-building, and the ploughing and reaping of the fields, thus relieving woman of the coarser kind of work. This form of household economy was long maintained, owing to the prevailing conditions of the time.

In the **second period** of development, there is an extension of the family, which is seen in the patriarchal family of the Romans, with their large number of slaves. Here the family needs were more numerous, and the exchange which took place between different districts was more in the nature of barter than of real trade. The similarity of men and their productions, as well as the paucity of their wants, gave no scope for the rise of an extensive trade; and, in consequence, there was scarcely any means of communications, no paved roads, etc. This state of



# COMMERCE IN ITS RELATION TO THE ECONOMIC SYSTEM



P. = Producer ; C. = Consumer ; T. = Trader ; C.T. = Collecting Trader ; D.T. = Distributing Trader ; I.T. = Intermediary Trader.

- I. No trade outside family group.
- II. Direct exchange by family group without intermediaries.
- III. Rise of the Trader as independent person.
- IV. Beginning of production for a market.
- V. Rise of a world market.
- VI. Extension of division of Labour and Intermediaries.



affairs, with its lack of intercourse, existed for thousands of years, and was retained by most peoples up to the Middle Ages. It is still to be found among many primitive races. A low state of civilisation, a scanty food supply, and great economic need are the evidences of this stage of commercial development.

The **third** and real form of trade first arose in dealing with strangers and under such conditions that progressive peoples were brought into touch with those of a lower civilisation. This was often due to the appearance of new commodities, which awakened desires and led to further exchange. Such intercourse sometimes assumed the form of direct exchange without the advent of a specialised trader, the goods being delivered at a fixed place from which the other party received another commodity in exchange. This still happens among some African tribes to this day. In the earlier stages of civilisation, princes, nobles, priests, high officials, and landowners exercised the functions of trade, and so, to a certain extent, might be regarded as the merchants of the time. For a long period, trade went hand in hand with robbery and deception, and was closely allied with smuggling. Hence the earliest forms of trade were carried on at great risks. However, the trader made his way not only in little known and out-of-the-way districts, but also amongst people who regarded him as a dangerous intruder, and therefore greeted him with deep distrust. In those early times, the trader required protection in a foreign country. This he sometimes purchased from the native prince, or at other times he might come under the protection of a powerful Government at home, or enter some form of society which aimed at protecting his interests.

Trade and religious institutions were, with advantage, conducted side by side, and religious festivals offered splendid opportunities for the trader on account of the large number of people who assembled at them. The religious nature of the festivals was a guarantee of peace and protection to the trader; whilst, in turn, his wares were an attraction to many who otherwise would never have attended them. It was with the object of securing protection that merchants travelled in caravans when trading by land, and on the sea they combined their ships into large fleets. Further development led to the establishment of protected centres as trading stations; factories or colonies on the main lines of



communication, from which the trader began to extend his power into the neighbouring territory ; and, with the development of trade with outsiders or with foreigners, the home trade became increasingly important. Out of the beginning of this simple system of exchange, there arose a regular trade and the gradual introduction of a common medium to facilitate exchanges. At first, all kinds of objects served for this purpose, such as shells, skins, cattle, gold dust, pieces of salt, dates, wheat, etc. ; but with the improvement in the treatment of metals, pieces of bronze, iron, gold, and silver were introduced. The values of these pieces of metal were first determined by weighing and afterwards by stamping, and they gradually became the universally accepted medium of exchange. A further great step of advance was marked by the introduction of weights and measures into trade.

With the growth of commercial enterprise, trade began to assume certain fixed forms, and passed into the **fourth stage** of development, in which production began to take place for some definite local market. This is sometimes spoken of as the *period of town economy*. Division of labour received a great impetus, and the branches of production began to be localised and to mark themselves off into agriculture, manufactures, and commerce. Fixed markets arose, and out of them there developed larger towns, which drew their supplies of food-stuffs, cattle, wood, etc., from the surrounding country districts in exchange for manufactured goods. In these towns, trade became a permanent feature, and soon divided itself into wholesale and retail. Here were started the earliest forms of money changing, dealings on credit, and a regular method of fixing prices. At this time, however, the wholesale trade, and that with distant parts, was relatively small as compared with the retail business. Trade with distant places was usually conducted by foreigners, who met periodically at markets and fairs to dispose of their commodities. These consisted chiefly of articles of luxury : ornaments, weapons, furs, fine manufactures, metals, etc., all of which were capable of being easily transported. In the conveyance of his goods from place to place, the merchant had to be accompanied by bands of armed men ; and, although the sea gradually lost something of its earlier character as a divider of peoples rather than a highway connecting them, shipping still assumed a dangerous and



unprofitable employment. At this time, there still remained among the masses of the people a certain mistrust of the foreign as compared with the home trader. In consequence, there arose in the towns a whole series of public and semi-public institutions for the regulation of commercial intercourse, the chief of which were the *Merchant Gilds*. Development, however, was considerably hampered by the imposition of heavy duties and restrictions on the freedom of intercourse. The prevailing conditions at this period were known as the Mercantile System, which is dealt with in greater detail in a later chapter.

The **fifth stage** of development (according to the diagram on page 16) is that of the evolution of the world market. In addition to the home trade extending over the whole area of a single country, there arises an international trade, which links together the nations of the earth through the medium of the *world market*. Goods are no longer transferred direct from the producer to the consumer, but are first passed through the hands of a collecting trader, who collects them from a producer and then passes them on to a wholesale dealer engaged on a centralised market. The latter then sells the goods to a distributing trader, who, in turn, passes them on to the consumer.

In the **sixth** and existing stage, it will be seen that there has grown up a host of intermediaries, through whose hands the goods usually pass before they reach the consumer. It is the complexity of the present commercial system that entitles it to special study as a subject separate and distinct from economics.

**COMMERCE IN RELATION TO OTHER SUBJECTS.** Although commerce finds its basis in economics, it is also closely allied to several other subjects, all of which are of the utmost importance for commercial life. The chief of these are—

1. Commercial Correspondence.
2. Arithmetic and Accounts.
3. Commercial Law.
4. Knowledge of Commodities.
5. Commercial Geography.
6. Economic History.

All of these specialised subjects are merely avenues, so to speak, which lead to the nucleus of the commercial course. This nucleus around which all these subjects seem to revolve is that



of "Commerce." The scope of these allied subjects may be briefly indicated as follows—

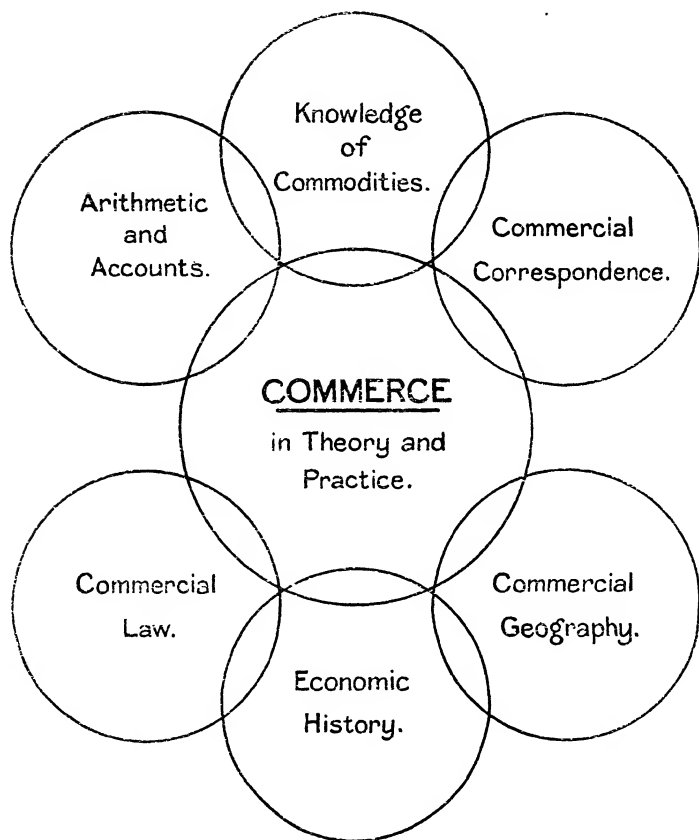
**Commercial Correspondence.** This subject should be studied in conjunction with the theory and practice of commerce, since it is merely another aspect of the latter subject (i.e. commerce viewed from the point of view of correspondence). Beginning with the writing of simple letters in reply to advertisements, it should proceed to deal with the various types of correspondence between the retailer and the wholesaler, such as the offer of goods, the prices current, opening up of business relations, letters connected with the settlement of accounts, and the use of the various documents connected therewith; correspondence in connection with banking, bills of exchange, etc.; contracts entered into by limited companies; letters concerning the appointment of travellers and agents; and transactions between the commission agent and customer. The branches which are auxiliary to trade should also be dealt with, such as transport and insurance, warehousing, etc., together with the preparation of such documents as the consignment note, bill of lading, insurance policy, documentary bills, and other forms in connection with the warehousing of goods. In short, the subject should deal with the whole sphere of commerce through the medium of correspondence.

**Arithmetic and Accounts.** This is the application of the principles and rules of arithmetic to accounts. Arithmetic is closely connected with every department of commercial practice. No transaction can be effected, no consignment of goods can be set in motion, no credit contracted nor business established, without the guidance and application of arithmetical processes. At every stage of business the services of arithmetic are enlisted. The person who wishes to become an efficient business man must, in the first place, learn to calculate and only a sure and rapid calculator will be able to place his undertakings on a sound footing. It should, therefore, be studied in conjunction with accounts and other important branches of commerce.

**Commercial Law.** This is that portion of English law which is more especially concerned with business transactions. The subject embraces a consideration of all those rights and obligations which arise in the conduct of commerce. Since the supreme object of the latter is the sale of goods, the most important branches of commercial law are those which relate to the sale of goods, the methods



## COMMERCE IN RELATION TO OTHER SUBJECTS



The central subject around which the commercial curriculum should revolve is "Commerce," which is itself based on Economics.



of payment for the goods, the transport and warehousing of the goods.

It is a well-known fact that much of the litigation which arises out of business transactions is the result of ignorance of the simplest rules of law. These rules are not difficult to learn and understand, and, with the increasing growth in the complexity of business, it has become an absolute necessity that a knowledge of commercial law in its main outline should form a prominent subject of study in the training of those who are preparing for a business career.

**Knowledge of Commodities.** This is the study of the chief characteristics of commodities, as well as the method by which they are acquired and used. It is concerned mainly with the most important raw materials and half-manufactured goods which enter into commerce. The leading physical and chemical properties of these goods should be known, as well as their sources of supply and the chief markets for the finished goods. This subject is, therefore, closely connected with economic geography and economics; and can be successfully taught only by the aid of various kinds of apparatus, such as a collection of different products, charts, and other graphical representations, as well as by a teacher with an all-round knowledge of natural science. According to their origin, three classes of commodities can be distinguished—

- (1) Mineral or inorganic.
- (2) Materials from plants, or vegetable productions.
- (3) Animal products.

The commodities of chief economic importance in a particular locality should be dealt with, and especially those upon which the students are dependent for their livelihood.

**Commercial Geography.** For the commercial student, geography is concerned with the description and explanation of the local differences upon which the existence of commerce has been shown to depend. It includes a study of the causes which help largely to determine the directions of roads, canals and railways, the location of mining and manufacturing industries, and the influence of physical facts in controlling the industrial activities of mankind. Moreover, the distribution and characteristics of the chief raw materials of commerce should be known, together with their influence upon trade and industry.



**Economic History.** The object of commercial history is to trace how, in the course of time, the conditions of commerce have changed among different people, and what circumstances and conditions have a permanent influence upon the development of trade. The commercial history of England begins by a description of its general economic condition at the time when the country first became known ; the surplus raw materials grown which could be exchanged for the products of other lands ; the prevailing means of communication ; the neighbouring countries with which trade has, from time to time, been carried on ; the influence of political treaties on the economic life of the people, and the circumstances which have gradually led to a change in industrial conditions. In short, the general development of agriculture, trade, and manufactures should be followed through the various periods.

Of course, a sound general education is indispensable as a preliminary to any form of business training. This view is definitely confirmed in the Interim Report of the Committee on Education for Salesmanship, which suggests that representatives of manufacturers and merchants trading in overseas markets, whether principals or professional salesmen, should possess the following qualifications—

(1) Good character ; (2) attractive personality ; (3) the capacity for making friends ; (4) suitable social qualities and manners ; (5) knowledge of human nature ; (6) good general education, including especially foreign languages ; (7) ability to investigate and report ; (8) knowledge of the goods or services they have to sell ; (9) knowledge of the country to which they are sent, of its language, customs, history, and peoples, and of the methods and facilities for doing business which prevail, including banking, credit, and transport ; (10) experience in selling ; (11) the confidence of the firm which they represent.

### TEST PAPER III

1. Upon what departments of economic study is "Commerce" chiefly based?
2. Account for the rise and continuance of a system of commercial intercourse.
3. Mention the six economic stages through which "Commerce" has passed.
4. What is the relation of Commerce to other subjects?
5. What in your opinion are the most essential commercial subjects? Outline the scope of each of the subjects you mention.
6. Discuss the relation in which "Commerce" stands to Geography, History, and Economics.
7. As the manager of a business, would you encourage your subordinates to qualify for advancement? How?
8. Estimate the importance to the trader of a knowledge of commodities.



## CHAPTER IV

### FUNDAMENTAL NOTIONS

IN the study of commerce, it is necessary that the student should first make himself acquainted with the principal terms used in economics. The following are some of the most important—

**POSTULATES.**—These are the assumptions which have to be made before a theory of economics can be developed for any given community. They may be conveniently classified as follows—

#### I. TWO FACTS OF PHYSICAL NATURE—

(a) *Law of Diminishing Returns*, i.e. as more and more units of capital and labour are applied to a given piece of land, the rate of increase of the return, after a time, begins to diminish.

(b) *Law of Increasing Returns*, i.e. equal additions of capital and labour applied to a business tend to produce a greater and greater proportionate return.

#### II. TWO PSYCHOLOGICAL FACTS—

(a) The utility of a commodity tends to diminish as the amount possessed increases.

(b) Satisfaction is required at a minimum cost.

#### III. TWO SOCIAL FACTS—

(a) The existence of legalised institutions in respect of property.

(b) Freedom of individual action within legal limits.

**WANTS.**—The function of human want is self-preservation, or the attainment of a higher state of development. The first aim of human existence is to obtain a sufficiency of the means of life. It is necessary to feed and clothe oneself, to procure fire and shelter, and to obtain those necessities without which life would be intolerable. The existence of want signifies that persons are in a state of desiring more of certain commodities, and the greater the desire the more urgent is the want. The existence of want leads to exertion and the endeavour to satisfy such want ; hence there arises a human struggle for existence and for the attainment of a state of well-being. Amongst the rudest and most uncivilised peoples wants are merely a means of self-preservation ; whilst among others they are the means to further development. The intensity of the wants is measured by the degree of dissatisfaction created by them in man,



and also by the quantity of goods which are required for the satisfaction of such wants.

**GOODS.**—Human wants are satisfied by means of goods, and goods are said to possess greater or less utility according to their power to satisfy human desires.

If nature supplies a "good" free, it is known as a non-economic good. If it satisfies a want and can be obtained only by human exertion, it is an economic good. In commerce non-economic goods, such as fresh air, sunshine, etc., do not enter into consideration. Economic goods consist not merely of material things, but also of immaterial, i.e. they may be the result of labour, but do not assume a tangible form. For our present purposes only those goods which are transferable are classed as economic goods. They consist of—

(a) *Non-material Goods*, e.g. services and intangible things such as goodwill.

(b) *Material Goods*, i.e. those things which assume a tangible form; such as houses, food, clothing, and machinery.

(c) *Paper Values*, i.e. goods which assume the form of paper and represent rights over other forms of wealth. These are subdivided into (1) documents of title, and (2) paper money. Documents of title include any bill of lading, dock warrant, warehouse-keeper's certificate, and any other document used in the ordinary course of business either—

(i) As proof of the possession or control of goods, or

(ii) As authorising or purporting to authorise, either by endorsement or delivery, the possessor of the document to transfer or receive goods thereby represented.

(d) *Coin*.

These four classes of goods constitute the commodities of commerce.

**MEASUREMENT OF GOODS.**—In the execution of commercial transactions it is necessary to have some contrivance by which the weight, length, surface, volume, capacity, and value of different goods may be compared. For this purpose some standard of comparison must be chosen, i.e. a common term which will enable two commodities to be measured and their attributes compared. In the British Isles, the standards of weight are the ounce, pound.



hundredweight, and ton ; of measurement, the inch, foot, yard, and mile ; the pint, quart, and gallon ; whilst the standard of value is the pound sterling.

A good system of weights and measures ought to have the following qualities—

1. *Accuracy.* The standard of measurement or of weight should have exactly the same qualities as any other standard of the same nominal value.

2. *Uniformity.* The same kind of weights and measures should be in use all over the country in which they have been adopted.

3. *Simplicity.* The system of weights and measures should be easily understood if it is to be of any real value in facilitating the exchange of goods.

4. *General Acceptance.* The weights and measures in use should be as widely known as possible. Many countries now use the metric system of weights and measures, and this is of great advantage to traders in such countries.

5. *Facility of Calculation.* The weights and measures adopted should be simple in calculation so that there shall be no undue waste of time. It has long been admitted that the British weights and measures do not possess this quality.

**VALUE.**—This is a relative term and refers to the quantity of some other thing for which a commodity can be exchanged. In reality, value is the feeling of esteem possessed by a person for a commodity, and is measured by the number of things he will give to obtain the commodity in question. In civilised countries a particular commodity is usually chosen to measure the relative values of other commodities, and this is known as money. The estimation of the value of another commodity in terms of money is known as the “*price*.”

**ENTREPRENEUR.**—In most business concerns it is the practice for one class of person to supply land, another capital, and another labour. The task of co-operating these factors is performed by the entrepreneur whose position in modern business is so important that it is necessary to regard him as a separate factor. He is the undertaker of business risks, and has to pay rent for his premises, interest on his capital, and wages to his workmen, perhaps long before he has produced the article which he intends to sell at a profit.

The entrepreneur of a sole trading concern ought to be so far



master of each section of his business that he can judge the efficiency and actual work of each of his employees, the quality of the raw materials, the efficiency of the plant, machinery, etc., as well as the condition of the finished and half-finished productions. At the same time he ought to have sufficient commercial education to guide him in his speculation, to enable him to anticipate expenses and output as closely as possible, and to render it possible for him to avail himself of the conditions of the market. Further, he should be able to compare the relative value of his own work with that of his competitors, to survey the ruling tendencies of the markets, to keep in touch with public taste, and to foresee economic crises. The importance of these different phenomena increases with the development of the undertaking, whereas in very small concerns the labour power of the entrepreneur and his family is often adequate for the conduct of the business. Every enlargement of the concern means the creation of a new activity which is handed over by the principal to a subordinate. The separation of functions has been carried so far that in many concerns the class bearing the risks of the enterprise are clearly separated from the organisation. The entrepreneur of a sole trading concern or partnership combines the functions of the organiser, of the capitalist, and of the undertaker of business risks. In a joint stock company, however, it is usual for the organiser to receive a fixed fee and for the risks of the enterprise to be borne by the shareholders. Hence, the shareholders are, in the strictest sense, the entrepreneurs of a company. In the case of a Co-operative Distributive Society, the entrepreneurs are the consumers themselves since they contribute the capital and undertake the risks of the business. In the case of a municipal undertaking the risks are undertaken by the ratepayers, and therefore they exercise the function of the entrepreneur. In such large concerns the responsibility of organisation is usually delegated by the proprietors to a managing director, who is rewarded by the payment of a fixed fee. In this case it would be a mistaken policy for the managing director to retain the simple tasks for himself, and to delegate the difficult and more important matters to his subordinates. In most enterprises it is usual, with every enlargement of the business, for the organiser to delegate part of his easier work, and to receive in return more difficult work, which will entail greater responsibility.



**DEMAND.**—The expression “Demand” usually refers to the added desires, expressed in terms of money, that a number of persons will give to obtain possession of a commodity. An individual may desire to possess an article, but unless he has the means with which to purchase it, his demand will not be effective. The only demand with which economists are concerned is “effective” demand, or the demand which will cause a commodity to be produced and to be put upon the market. Effective demand is further divided into “demand in the abstract” and “demand in the concrete.”

Demand in the abstract means the desire to possess coupled with the power to purchase, and concerning demand of this kind the question to be asked is whether there is or there is not a demand for a particular commodity in the community. It may be said that there is a demand for bicycles in England, because people are desirous of possessing them and are willing and able to pay for them. This is abstract demand. Concrete demand is the desire to possess an article *at a price*, and indicates the quantity of the article which will be bought at the price. There may be not only a demand for bicycles in England to-day, but there may be a demand for 10,000 bicycles at £8 each, which would be demand in the concrete.

**Elasticity of Demand.** When a small change in the price of a commodity causes a great change in the amount bought, the demand is said to be *elastic*. For example, if a commodity is offered at 2s. and fifty people purchase it per week, and the price is lowered to 1s. 11d., and 200 people buy it, then the demand for that commodity is elastic.

An inelastic demand for an article is one in which a considerable change in price fails to affect the demand much. For example, the demand for steam-engines is inelastic since a small alteration in price will have little effect upon the demand.

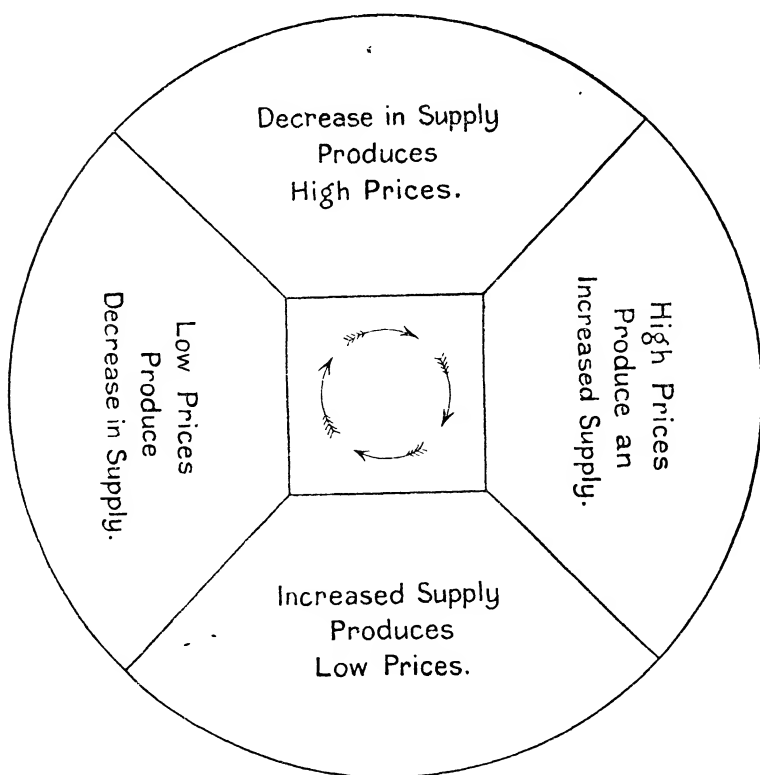
**SUPPLY** is the quantity of a commodity which will be offered for sale at a price, and is always concrete. Thus the equation of supply and demand refers to the tendency to equate the always concrete supply to the concrete demand.

The quantity of bicycles offered for sale at £8 each tends to be equal to the quantity of bicycles that will be purchased at that price.



The two forces must now be combined in order to understand their operation. Demand depends upon the supply price of a commodity and increases when price goes down. In other words, the greater the amount of any commodity or service offered for sale in any market, the less the price that can be obtained per unit of it, and *vice versâ*. Supply also depends upon price, diminishing when price seems materially to be less than the sum total expenses of production, and increasing when price is higher than cost of production. The combination of the laws of supply and demand as they would operate within the limits of what is called a market is shown in the following diagram—

## DEMAND AND SUPPLY IN RELATION TO PRICE





The interaction of the laws of demand and supply may be summed up as follows—

Increased demand raises prices.

The rise in price stimulates supply.

Increased supply leads to a fall in prices.

Fall in prices increases demand.

Fall in demand lowers prices.

Lowered prices diminish the supply.

The diminution of supply raises prices.

The rise in prices diminishes demand.

The entire movements of production and industry are regulated mechanically by prices. An increased demand raises prices ; this rise restricts demand and stimulates supply. The opposite effect gives an increase of supply followed by lower prices which in turn stimulates demand.

**MARKET.**—A market for a commodity may be defined as that area, large or small, within which every portion of the supply is equally available to each portion of the demand. Markets may be of various sizes according to the nature of the commodity, and the nature of the person demanding the commodity. In the case of securities such as consols, the market includes practically the whole civilised world, since there is only one price, whereas in the case of articles like bacon, there may be several different prices and therefore different markets in the same street. Again, a man's market for clothes may consist of a single tailor's shop because he has no desire to go anywhere else. This tailor may have made clothes for the ancestors of this man, who has continued to limit his purchase of clothes to that particular shop. But when the order is given to the tailor, he will have a market for the cloth out of which to make the clothes and that market may be the West Riding of Yorkshire. There will be a different kind of market for the retail clothes and the wholesale cloth. There is an important law of the market known as the Law of Indifference, which says there can be only one price in the same market. Jevons enunciates this law in the following words: "In the same open market at any one moment there cannot be two prices for the same kind of article." This law depends upon the absence of any form of monopoly, and also on the degree of divisibility of the particular



commodity. If every portion of the supply is equally available to the buyer there is no reason why he should pay 2s. 6d. for something which he can purchase for 2s. In the same market, then, there must be only one price.

People sometimes dispute the operation of this law. They say the same article can be bought at different prices at different places. But these different places are separate markets according to the definition given above. The supply which exists in one place may not be available equally to the demand which is experienced in some other place, and hence the difference in price. The supplies exist in different markets.

**MARKET AND NORMAL PRICE.**—If an entrepreneur sees a probability of getting a price greater than the total expenses of production, he will increase the output of that particular commodity ; but if he thinks he will not get as much as the total expenses of production, including a fair profit, then he will restrict the output. The cost of production of a given quantity of the supply determines the least the sellers can profitably afford to take, and the intensity of the demand for the commodity the most buyers will give. When the demand price is just sufficient to carry off the available supply at this minimum or supply price, demand and supply being in equilibrium, the point of normal price is said to have been reached. If the producer takes less than this normal price he will incur a loss or make no profit, whereas if he takes more, he will receive more than the average rate of profit.

The market price continually varies about this normal price or point of equilibrium. If demand is greater than this supply then the market price is greater than the normal price, and vice versa.

Thus supply, demand, and price are three great forces in equilibrium, i.e. the triangle of forces mutually acting and reacting upon one another, so that the smallest change in one at once affects a change in the other two.

**CONTRACT.**—A valid contract is an agreement and promise enforceable at law. For the existence of such an agreement there must be—

- (1) An offer ;
- (2) An acceptance of the offer ; and
- (3) A certain binding force attached by the law to enforce the promise thus formed. This force creates what is called an obligation



or legal bond, which, when broken, causes the contract to be discharged.

*Offer and Acceptance* denote two or more persons being of one mind, otherwise no agreement ensues. Doubt or difference is not possible where there is agreement. The offer must be accepted before any contract is made. Both parties must have the intention communicated to them, and the agreement must be such as to affect the legal relations of the parties.

A contract is, therefore, an agreement enforceable at law between two or more persons by which rights are acquired by one or both parties to acts or forbearances by the other or both.

**The Essentials of a Contract** are as follows—

(1) A distinct communication by the parties to each other of their full intentions, the one to offer and the other to accept that offer in full without any restriction not expressed in the offer.

(2) The presence of evidence sufficient to show that the parties wished to affect their legal relationship. This takes one of two forms—

(a) Form, e.g. a contract under seal.

(b) Consideration, i.e. some gain or profit to the party making the promise in return for his promise. For instance, A and B agree that A will sell his horse to B for £20. Hence, £20 is the consideration for the horse.

(3) The parties must have legal capacity to contract.

(4) Offer and acceptance must be genuine.

(5) The objects of the contract must be perfectly legal.

When these five elements co-exist the contract is valid. The absence of one of them makes the contract void, voidable, or unenforceable.

A *Void Contract* is destitute of legal effect and neither one party nor the other can enforce it.

A *Voidable Contract* is capable of being carried out or not, at the option of one of the parties to it.

An *Unenforceable Contract* is perfectly legal, but being incapable of proof in a Court of law through some technical defect, it is called a contract of imperfect obligation, and is in the true legal sense no contract at all.

In general, all persons may be parties to contracts, but no person



can contract with himself in a different capacity, as there must be an agreement of minds. Furthermore, parties must be capable of contracting at the time they enter into the undertaking, for without capacity there can be no assent, and no understanding. Hence, before a party can bind himself to a contract, he must be able to understand its nature. When one of the parties is mentally incapable of contracting, the contract is void. Beside the requisite of capability, parties to contracts must *exist*. If they purport to be natural persons, they must be living. There can be no legal contract with a *fictitious* person. In the case of an *artificial* person, such as a corporation, it must have a legal existence to entitle it to contract.

Persons with defective capacity to contract are (1) infants, (2) aliens, (3) lunatics and drunken persons, (4) married women, (5) corporations. In all these cases, however, there are qualifying circumstances. In the case of married women, for example, many anomalies of long standing have been removed by the Law Reform (Married Women and Tortfeasors) Act, 1935.

#### TEST PAPERS IV.

1. What are the chief "Postulates" of Economics?
  2. Explain the function of "want" in the economic system.
  3. Distinguish between "economic" and "non-economic" goods.
  4. What qualities should be possessed by a good system of weights and measures?
  5. "Value is a relative term." Do you agree with this statement?
  6. Is there such a thing as "intrinsic value"? Give reasons for your answer.
  7. Explain the relation of the "Supply" of a commodity to its price.
  8. What is meant by "Elasticity of demand"? Mention cases of commodities the demand for which is "inelastic."
  9. What is the function of the *entrepreneur* in modern business?
  10. Explain carefully the functions of the employer in the modern industrial system. Illustrate by reference to the different types of business organisation in the British Isles.
  11. Describe a perfect market. Give examples of both perfect and imperfect markets. Discuss the case of the Labour Market.
  12. Distinguish between "market" and "normal" price.
  13. What are the essentials of a valid contract?
  14. Explain how every agreement can be analysed into an "offer and an acceptance."
- A gets into an omnibus, and, after travelling some distance, pays his fare and gets out. Show that there was a contract between the 'bus company and A, pointing out the "offer and acceptance."
15. Give three instances of persons who do not possess full contractual capacity.



## CHAPTER V

### AGENTS OF PRODUCTION

**AGENTS OF PRODUCTION.**—It has been seen that the economic activity of man is directed towards the production of goods, and that production is the conferring of utility on materials supplied by nature, with the object of satisfying human needs. The leading motive in production is the economic consideration which aims at the creation of maximum utility with the minimum expenditure of effort, and a business is said to succeed economically when the value of the return is greater than the total value of the efforts incurred when measured in terms of money. An undertaking is, therefore, productive in the economic sense when it creates new values or increases the values of already existing goods. Hence it will be seen that not only are the extractive and manufacturing operations productive, but also the activities between production and consumption, viz. commerce. The chief requisites in production are the resources of nature and human labour, and capital, without which the creation of wealth is scarcely possible. The last-named factor is of great importance at the present day. These three agents—nature, labour, and capital—are often spoken of as the “factors of production,” labour often being referred to as the personal, and nature and capital as the material, factors.

**NATURE.**—The whole of production is, in the last resort, dependent upon nature. Of the greatest importance to industry are climate, land, and the distribution of water, for by them is largely determined the character and extent of a country's production.

*Climate* depends chiefly upon the position and configuration of the country. Continental places are subject to greater extremes and smaller rainfall than districts situated near to the sea. For instance, in Russia the rivers and seaports are closed for months in winter by ice, while those of the Atlantic coast in corresponding latitudes are always kept open by the influence of the comparatively warm sea-water. Climate has a direct influence in determining the variety, the quantity, and the quality of products in a given area; and indirectly, it exercises an influence upon the nature and extent of man's needs. A further effect is its determining



influence on the disposition and character of man, which reacts upon his power to exploit the resources of nature.

The chief natural factor which enters into production is *land*, for it serves as the home and the workshop of man. In an agricultural community it determines the entire economic and social relations of the people. The configuration of a country, i.e. the form and arrangement of its mountains, valleys, high and low lands, determines the size and directions of its rivers, and the value of its soil for cultivation. In many countries, the State pays particular attention to the cultivation of the soil, and seeks to develop the efficiency of this factor through legal and economic measures. In this respect may be mentioned the various forms of land ownership which exercise an undoubted influence on the total product of industry. In production, not only is the fertility of the soil and its suitability for agricultural purposes important, but also its riches in minerals and natural power. A discovery of gold, silver, or oil may bring a rush of people to a barren region, difficult of access. While these natural deposits last, railways are constructed, the soil is improved for agriculture, and towns are built ; and when the supply is exhausted the result may be a self-supporting settlement permanently established and in full communication with the world. Thus, the position and industries of large centres of population are usually determined by the existence of natural resources.

The economic importance of *water* consists partly in the existence of the water itself, and partly in the useful things contained therein, such as common salt, fish, and plants ; and partly in its capacity for transport and as power for the conduct of manufactures. Water is one of the most important of the necessities of life, and human settlements are only possible where it exists or can be obtained in sufficient quantity and of good quality. Moreover, in consequence of its varying constituent properties, its existence in certain qualities is important for the conduct of brewing, fishing, dyeing, tanning, and for purposes of healing certain maladies.

Thus, the production of a country is due largely to the existence of natural resources : the nature of the climate ; the relief of the land ; the fertility of the soil ; the geological formation ; the configuration of the coast-line, and situation with regard to other countries.

**LABOUR.**—Labour is the application of the mental and physical



powers of man to the attainment of an economic result. Without labour, production is impossible ; and, therefore, the extent of a nation's wealth is materially dependent upon the amount of work which is done by its people. Man's own necessity forces him to labour, and the possibility of being able to satisfy his needs acts as a stimulus for him to put forth his efforts. This mainspring to activity operates to a much smaller degree where the labourer has only a limited number of wants or where he is unable to depend upon reaping the fruits of his labour. This inducement to activity increases with the intensity and extensiveness of human need, and with the certainty of receiving an adequate reward for services rendered. The efficiency of the individual worker is determined by his physical, mental, and moral capacity, as well as by the amount of experience he has received of the particular kind of work which he has undertaken. The chief factors which determine the extent of the national labour power are the relation of the number of workers to the whole population, the average working capacity of the labouring classes, and the general characteristics of the people. The earliest and simplest form of the development of the natural resources by labour was the collection and appropriation of wild plants, the acquiring of the raw materials found on the surface of the earth, and the catching of wild animals. With the increase of population, labour began to be applied systematically to the production of raw materials, and thus man engages in agriculture, cattle rearing, and afforestation. With the greater control over nature, he next turned his attention to the working up of raw materials into a form fit for the direct satisfaction of human needs. This gave rise to handwork, manufactures, and the transference of goods either directly to the consuming public as in the case of the retail trade, or in large quantities for re-sale as in the case of the wholesale trade. Finally, there are the workers engaged in rendering personal services of all kinds ; such are teachers, doctors, etc.

**Division of Labour.** The increase of the efficiency of labour by means of division of labour is specially important in regard to the total output of production. It is the distribution over many businesses or persons of work which was formerly executed by a single business or person. In the course of industrial development, there has taken place the separation of the extractive from the



manufacturing industries, and the division of the latter into a number of different businesses. For example, the work of the smith has gradually been subdivided into that of the blacksmith, the nail-smith, the tinker, the cooper, etc. Finally, these different occupations have been separated into a number of stages, and each man confines himself, as far as possible, to a single stage, instead of making the entire article himself. In the making of pins, for example, the wire passes through a whole series of hands before reaching the last stage of the finished product. All these examples come under the heading of division of labour, the chief advantages of which are—

- (1) The development of greater skill on the part of the worker.
  - (2) The lightening of human toil.
  - (3) An increase in the number of improvements, discoveries, and in the inventiveness of the people.
  - (4) The saving of time and materials in the training of workers.
  - (5) The possibility of delegating tasks according to ability, etc.
- For example, weak or unskilled persons may be set to do the simpler kinds of work.

Thus, by means of the application of the principle of the division of labour there results an increase in the quantity, variety, and cheapness of the products.

In contrast to these advantages may be mentioned the following disadvantages—

- (1) The worker tends to become more one-sided and there is little variety of occupation.
- (2) If the task is a very simple one there is no opportunity for the development of inventiveness.
- (3) If the pace of the worker is set by a machine, there is an increase of nervous strain on the worker.
- (4) Since all the different stages have to be kept fully employed, the work of organisation becomes increasingly difficult.

Generally speaking, the development of industry is accompanied by an ever-increasing division of labour and especially by greater subdivision of the stages through which a product has to pass before reaching a finished state. In the modern shoe factory, for instance, labour is divided into almost one hundred different processes.

**CAPITAL.**—In ordinary life the word *Capital* is connected with



quite a number of different conceptions. To the business man it indicates a sum of money lent out at interest, or it may bring to his mind the actual form which capital assumes in a business ; such as land, buildings, machinery, money, or claims upon debtors. Likewise, in a scientific sense, the term " Capital " has many different meanings.

**Production Capital.** In the first place, it will be well to examine the meaning and function of capital as a factor, along with labour and natural resources, in the production of wealth.

If the student will recall to mind any examples of production with which he is acquainted, it will be seen that human effort seldom, if ever, operates directly upon the materials freely supplied by nature. In the production of most goods, some means of assistance to hand labour is provided in order to get the best results. The most important of such auxiliaries are the many kinds of tools and implements which have been brought into use by man through many thousand years of development, ranging from such primitive forms as the stone axe to the complicated automatic machinery of our modern factories. Labour is further assisted by the already existing supply of raw materials, the building in which manufacture and construction take place, the transport facilities, by means of which raw materials are conveyed to the place of manufacture or of consumption, the improvements of the soil by, e.g. drainage and fertilisation. All these means of assistance are the results of past labour which have been saved up and can now be used to assist further production. They include every description of assistance to man's labour which has not been supplied freely by nature, and are known as capital. Capital then is the sum total of those means which co-operate with man in the production of wealth, which are not freely given by nature but are themselves the product of human labour. Capital co-operates in every stage of production, irrespective of the legal relations of the persons using it, or whether it be owned by an individualistic or by a socialistic undertaking. In this sense it is known as Production Capital, which is the ordinary use of the term in economics.

**Forms of Production Capital.** Production Capital assumes many different forms, the chief of which may be grouped as follows—

(1) Raw materials ; such as corn, flax and ore, out of which are made flour, linen, and iron.



(2) Auxiliary materials which are used in production without forming a visible part of the new product ; e.g. coke in the smelting of iron, and manure in agriculture.

(3) Implements of production ; such as tools, machines, utensils, etc.

(4) Buildings in the service of production ; such as dwellings, factories, workshops, stables, warehouses, waterworks, etc.

(5) The system of exchange, together with the institutions connected therewith.

(6) Improvements of the soil ; such as drainage and irrigation schemes, which render production more efficient.

(7) Beasts of burden.

The greater the number of such forms of Production Capital, the more varied is the output of new goods. The stock of Production Capital existing at any given moment of time determines the output of the immediate future. It is, therefore, of great importance for the general welfare of the whole population that the stock of Production Capital should not be permitted to diminish, but should be replenished according to the amount consumed in the process of production. The increase or diminution of capital in a community is a matter of great economic significance.

**Revenue Capital.** When it is regarded, not from the point of view of production, but from that of the individual, capital has a different meaning. According to this meaning, capital is that wealth which enables its owner to earn an income, and is known as Revenue Capital. The utilisation of wealth with the object of earning an income presupposes an economic system based upon exchange, and the existence of private ownership as a legal institution. Revenue Capital is not to be found, therefore, in every stage of economic development, but is the result of historic evolution. The basic fact that an income may be produced from the ownership of wealth, if used in production, seems to have dawned upon many people at the period when towns first began to develop and especially with the advent of large scale production. The classification of capital in this sense is partly legal and partly historical. In addition to the goods which constitute Production Capital, the term Revenue Capital includes all other forms of wealth which are the means of producing an income ; such as the trader's stock of goods, which are ready for sale and from which he expects to earn an



income ; the money to be lent by the banker ; waste land from the sale of which, as building land, the owner expects to derive an income.

The difference between Production Capital and Revenue Capital is important for the appreciation of the true meaning of many economic phenomena. It may be said that a nation is the richer, the greater the supply of Production Capital. This ensures a larger return to production and therefore enables the needs of the whole community to be satisfied to a greater extent. On the other hand, Revenue Capital only procures for its owner the means of satisfying his wants and in many cases is not accompanied by a general increase in economic well-being ; e.g. speculators often seize waste land in large towns which is suitable for building purposes and by skilfully withholding it from the market, cause its price to be raised. Although profitable to the owner, such Revenue Capital is prejudicial to the communal interests, since it leads to the increase in the cost of production. Again, the fact that goods have to pass through the hands of a large number of intermediaries, each of whom expects to make a profit, is injurious from the economic standpoint since it will ultimately lead to an increase of prices to the community in general.

**Auxiliary and Remuneratory Capital.** Another division of capital is into Auxiliary and Remuneratory.

Auxiliary Capital is that which specially assists the labourer in production ; e.g. tools, machinery, etc. ; whilst Remuneratory Capital is that which is used for the payment of the worker's wages. If the elements of capital be divided into tools, materials, food, clothing, and shelter, it will be seen that the first two are used to assist the labourer in production, whilst the last three are used in his remuneration. Thus—

Tools	}	Auxiliary Capital.
Materials		
Food	}	Remuneratory Capital.
Clothing		
Shelter		

**Fixed and Circulating Capital.** Adam Smith divided wealth or " stock " into two classes—that which is not capital and that which is capital. The non-capital stock is that which is in a form to satisfy wants directly ; that is, goods which afford a direct sustenance to the workers, such as food, clothes, house-room, etc. This is termed **Consumption Capital** by Professor Alfred Marshall.



**Fixed Capital** is that which can be used a number of times without complete exhaustion of its utility, but from which the value of each use goes to increase the value of new products.

**Circulating Capital** is that which is completely changed in form or consumed by one use, its value passing over entirely into the new product.

The classification of "wealth" may, therefore, be represented as follows—

### CLASSIFICATION OF WEALTH

Wealth.	{	Non-capital or Consumption Wealth.		{ Reserved for immediate Consumption and yielding no Revenue.
	{	Capital	Fixed	{ Machines, Trade Buildings, Improvements in Land, Acquired Abilities of the Members of Society.
			Circulating	{ Money, Provisions awaiting Sale, Materials not yet made up, Finished goods awaiting Sale.

The goods awaiting sale shown as Circulating Capital will, when sold, pass into the class marked Consumption Wealth, since they will be goods for immediate consumption.

In fact, all the Circulating Capital, except money, will find its way ultimately into the first of the above classes. In a certain sense, money is a tool just like a railway wagon, or a canal barge. It has to be maintained, and every expense incurred in such maintenance is a net deduction from the available wealth of the community.

The difference between Fixed and Circulating Capital may be further illustrated from the following simple Balance Sheet—

### BALANCE SHEET

<i>Liabilities.</i>		<i>Assets.</i>	
	£		£
1. Share Capital . . .	500,000	1. Land . . .	100,000
2. Reserve Fund . . .	285,000	2. Buildings . . .	50,000
3. Creditors . . .	300,000	3. Machinery . . .	200,000
4. Bills Payable . . .	70,000	4. Implements . . .	10,000
5. Undistributed Profit .	50,000	5. Office Fittings . . .	1,000
		6. Raw Materials . . .	120,000
		7. Finished Goods . . .	80,000
		8. Debtors . . .	530,000
		9. Bills Receivable . . .	60,000
		10. Cash . . .	54,000
	<u>£1,205,000</u>		<u>£1,205,000</u>



The Assets side of the Balance Sheet indicates capital in a certain state of liquidity, whilst the Liabilities are indicated according to their origin.

According to the form of assets, capital may be grouped into two large classes. Nos. 1-5 are Fixed Assets, since they are intended for permanent use in the business. Nos. 6-10 are items of capital, which are not for permanent use, but form part of the turnover. They are known as the Circulating Capital. By turning over the Circulating Capital, profit can be made. For this reason, the chances of success increase the greater the proportion of Circulating Capital to the Fixed Capital.

The Liabilities side shows how the capital has originated. It is made up partly of the undertaking's own capital (Share Capital, Reserve Fund, Undistributed Profit), and partly of outside items (Creditors, and Bills Payable). The former is the only capital which is at the disposal of the business for a long period of time, whilst the latter may be regarded as short period obligations.

**Social Capital.** This refers to those possessions which can be regarded as the "Capital" of a body of persons, such as a municipality or nation, but not of any particular individual. The tramway service, waterworks, gasworks, picture galleries, etc., are examples of the Social Capital of a municipality, whilst the Post Office, the telephone and telegraph services, are part of the Social Capital of the nation.

**Capital from the Accountant's Point of View.** Capital as viewed by the accountant is an amount of wealth ventured by the proprietors of a business for the purpose of carrying out some enterprise. It is often regarded as a fund, and this is a convenient way of describing it so long as its limitations are appreciated. The word "fund" means something placed at the bottom, and therefore it is something which will seldom be touched. As applied to such firms as insurance companies and banks, this would, as a rule, be an accurate description, for the capital subscribed by these firms is practically all invested and is the basis upon which their credit is founded. Capital in this sense may be regarded as a fund which would practically never be touched at all.

In ordinary business concerns, however, the capital is not funded in the sense that it is put at the bottom of a chest and never touched so long as things are working smoothly, but it is a fund which is to



be administered, and on the manner in which it is administered depends the success of the operations. Hence the use of the term "fund" as applied to an ordinary business concern is not a particularly appropriate one.

The capital subscribed in the case of an ordinary business concern has to be accounted for to those who have subscribed it, whether there be one or many. It is for this reason that capital is treated as a separate entity in the books of a firm.

The business which starts with no property or obligations of any kind is first supplied with wealth in the form of capital, for which a corresponding obligation to the subscribers is shown in the firm's books. Then comes the question of the administration of this wealth which has been acquired for the purpose of the business. The business operations will consist almost entirely of the exchange of commodities of different kinds with the object of making a profit. Since this process involves a continual exchange of goods, the term "fund" used in this connection is rather a misleading one, for some of the exchanges will be advantageous and some disadvantageous, so that the actual capital of the undertaking will be a continually varying quantity. By the aid of credit operations the business house will be able to acquire a considerable number of commodities without giving anything in exchange for them at the time, except an undertaking to pay for them later. As soon as the operations of the business begin, the tendency will, therefore, be not merely to exchange the capital subscribed for commodities, but the business will also acquire other commodities in exchange for the obligation to pay for them at a later date.

Hence, it may be supposed that a firm starts with no assets and liabilities, and after the capital has been subscribed there is a liability to the subscribers on the one hand, and an equal quantity of commodities on the other hand. Very soon the stage is reached when the value of the commodities exceeds the capital, since some of the goods are purchased on credit. There will then be further liability towards the parties for the commodities acquired. However, the total value of all assets will at all times exceed the total values of liabilities, although the totals will, in fact, be continually varying. The aim of the business is continually to effect exchanges which will be to the advantage of the firm, and in this process *profits* will be made. The commodities bought for a certain amount will be

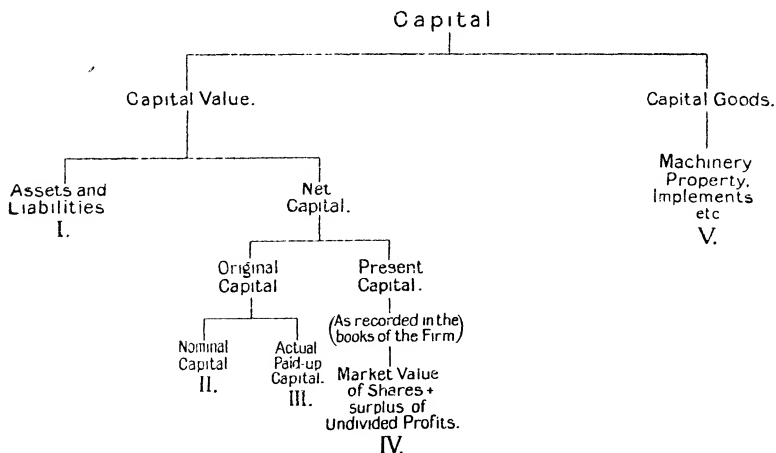


exchanged for a larger sum, and thus the total of the assets will be increased without effecting any corresponding increase in the firm's liability to strangers, or increasing the original amount of capital subscribed by proprietors, but not without increasing the total amount of the firm's liabilities. It must be remembered that the business has to account not merely for the capital originally contributed by its proprietors, but also for all the profits made out of the administration of the capital, so that every time the administration of capital results in an increase of assets, the process involves a liability to account to shareholders for an equivalent amount of profit. The total amount of assets possessed will always equal the amount of liabilities to all parties and these may be subdivided into—

- (1) Those to be accounted for to strangers.
- (2) The amount of capital originally ventured by the proprietor.
- (3) Liability for profits earned.

It may be convenient to think in terms of subtracting the amount of the liabilities from the assets and then to speak of the remainder as representing the net assets available to meet the capital and profits. This view of capital may best be illustrated diagrammatically as follows—

### CAPITAL OF A BUSINESS





**Different Meanings of Business Capital.** From the above it will be seen that the capital of a business has at least five separate meanings—

(1) The total assets and liabilities of the business regarded respectively as positive and negative capital.

(2) The nominal or face value of the capital, e.g. company shares issued at £10 each, of which £2 only is paid.

(3) The original paid-up capital.

(4) The present accumulated capital which consists of the market value of the shares together with any undivided surplus of profits.

(5) The tangible property of the firm which is used in the production of further wealth.

The object of conducting the business is to earn profits for the advantage of the proprietors, and therefore the normal attitude of the proprietors towards these profits is that they are entitled to withdraw them for their own private purposes. Some concerns, however, find that the demands for further capital in the business can best be met by the distribution of only a part of the accrued profits, and thus retain the remainder in the business. Hence these profits correspond to the business capital.

Again, it does not necessarily follow that the various proprietors will be entitled to share profits in exactly the same proportions as those in which they have shared capital. In the case of a sole trader, one person only is interested in the profits, but in the case of a partnership each member subscribes according to mutual agreement. The law of partnership provides, however, that, unless there is an agreement to the contrary, each partner has a right to share equally in the profits with the other partners. This is a recognition that it is not capital alone which creates profits, but capital in combination with brains, and therefore the amount of capital subscribed is by no means necessarily the only factor which determines the reasonable distribution of profits. Unless partners are willing to divide the profits equally they must make such an agreement in advance.

In the case of companies where the individual shareholder does not, as such, take any part in the active management, and the management of the business is in the hands of the directors who are paid fees for their services, the assumption on the part of the law is, that profits will be divided *pro rata* among the members. Every



company is allowed to make its own internal regulations, but in default of its making any regulations, a schedule known as Table A applies, and this contemplates that profits are to be divided among the members in proportion to the amount of the capital which they have respectively subscribed.

**Proprietor's Capital.** A considerable proportion of the capital employed by business enterprises must be found by their proprietors. In the case of a sole-trading concern, the capital will be provided by the founder of the business from his own savings, and will be represented in his books of account as the difference between the total assets and liabilities on the date of commencing business. This capital will be increased by the profits and diminished by the losses of the business. In the case of the partnership the position is exactly the same except for the fact that each partner has his individual capital account. In addition to the direct investment of capital by the owners of a business, capital may also be provided by allowing profits to accumulate in the business, usually in the form of reserves, or in the form of an undivided balance of profit and loss account.

In the case of the joint-stock company, the capital is usually raised by a general appeal to the investing public for subscriptions. Such companies divide their capital into a large number of fractional parts called shares, each one of which has usually the same nominal value, the most common denomination being one pound. The rights which attach to the owners of these shares vary according to the conditions laid down by the company at the time of issue, and it is open to the company to issue more than one class of share. The following are the chief classes—

1. *Non-cumulative Preference Shares.* These usually rank first both as to payment of dividend and return of capital. Preference shares may be issued carrying the first of these preferences only, but if they carry both, then (a) the fixed rate of interest attached to the shares must be paid out of profits before the ordinary shares rank for dividend; (b) in the event of the company going into liquidation, preference capital has the right to prior payment before other classes of shares, should funds for repayment be available after payment of debts.

These shares carry a preferential right to dividend out of the profits of each year only, that is, so far as profits are available



to pay the dividend. The decision as to what profits are available rests with the directors.

2. *Cumulative Preference Shares.* With this class of share, the preferential rights to dividend accumulate from year to year in the event of the non-payment of the dividend, the arrears of one year being carried forward to the next. There may, of course, be several classes of cumulative preference shares, each ranking for dividend in a certain order.

3. *Participating Preference Shares.* In addition to the advantages attaching to cumulative preference shares, these shares carry a right to a fixed share in the surplus profits after payment of the fixed dividend to which they are entitled, usually after a certain minimum has been paid on the subordinate classes of shares.

4. *Redeemable Preference Shares.* A company may, if so authorised by its Articles, issue preference shares which are, or at the option of the company are liable, to be redeemed. No such shares may be redeemed except out of the profits of the company which would otherwise be available for dividend, or out of the proceeds of a fresh issue of shares made for the purpose of the redemption. Such shares can be redeemed only when fully paid.

5. *Ordinary Shares.* The bulk of the shares issued by most limited companies are of this class. Ordinary shares carry no special rights as to dividends or capital repayment. Generally, they are entitled to the surplus profits remaining after the prior fixed dividends, enumerated above, have been satisfied.

6. *Founders' Shares.* These shares are usually issued as fully paid to the promoters, or managers, of the issuing company. As regards dividend, they usually stand aside until an agreed dividend has been paid on the ordinary shares. Though generally few in number and insignificant in nominal value, the voting powers which they command and the profits they share are often considerable. They are not popular with the investing public, since they do not always lead to prudent management, the holders being usually desirous of dividing all available profits without much regard for the prudent building-up of reserves.

7. *Co-partnership Shares.* These shares are sometimes issued to a company's employees in order to give them an interest in the concern. Frequently such shares carry no voting power. They are



usually entitled to the same dividend rights as the ordinary shares, but their transfer is usually under the control of the company.

**Outside Capital.** In addition to the capital which is contributed to a business by its proprietors, an undertaking also obtains a considerable proportion of its resources from outsiders. These contributions of capital may take the form of direct loans to the concern for varying periods of time, or indirect loans in the form of trade credit. The greater part of this capital is short-term capital, so that its nature is constantly changing. The chief sources from which it is obtained are—

1. *Debentures.* In its simplest form a debenture consists of nothing more than a mere acknowledgment of a debt given to a creditor. It may, however, contain provision for the giving of security to the creditor, and in such cases the documents are known as *mortgage debentures*. In form, the debenture is similar to the share, being transferable and of low nominal value, but the legal positions of the holders are very different. A shareholder is a proprietor of a company, whereas a debenture-holder is merely a creditor. Debentures may be either redeemable or irredeemable. The former are issued subject to the condition that the company shall redeem them on or before a certain date, whilst the latter have no fixed date for redemption.

2. *Bank Loans.* A second important source of outside capital is the loans and advances made by commercial banks. This method of finance will probably be resorted to if a limited amount is required for a comparatively short period of time. Generally speaking, British banks are willing to provide some of the circulating capital required for business purposes, but are not prepared to lock up their resources in fixed capital assets. This type of advance is usually made against some form of security such as (a) gilt-edged securities; (b) shares in reputable limited companies; (c) personal guarantees of directors; (d) mortgages of land or buildings.

3. *Trade Suppliers.* Although obviously trade suppliers are not specifically engaged in financing those business houses with which they deal, in actual practice they frequently provide an undertaking with a considerable amount of circulating capital. When they supply goods on credit to traders, they are in reality placing some of their capital at the disposal of the trader for the term of the period of credit, and this capital can be utilised for the purposes of the



business. Provision of capital in this way is usually a very informal matter, being based upon the personal knowledge which the supplier has of the trader receiving it. This method may appear to be an easy way of obtaining working capital, but very frequently it proves expensive. The person advancing it may recoup himself by charging an extra price for the goods which he sells, or by demanding other concessions.

### TEST PAPER V

1. What are the agents of production? Explain how "Nature" aids in the work of production.

2. "Man creates utilities, not things." "Production consists in the creation of values." Explain these quotations, bringing out clearly the function of Labour.

3. Discuss the following statements—

"Production is controlled by the capitalist."

"Production is controlled by the *entrepreneur*."

"Production is controlled by the receivers of income."

4. "Modern production is group production."

"Production with capital is a roundabout process."

Explain and discuss these statements in relation to each other.

5. It has been said that "division of labour" implies "combination of labour." Consider the relation between division and combination of labour, with special reference to the way in which each tends to develop the other.

6. In what respects does Labour differ from a commodity, and the Labour Market from a market for goods?

7. Give some of the reasons—other than habit and want of intelligence—why division of labour is not carried much further than is actually the case.

8. Sketch shortly the chief features of the actual "Division of Labour" existing in any modern society. How far is there "international division of labour"?

9. Explain the meaning of the terms "Money," "Wealth," and "Capital."

10. If shown a certain commodity and asked whether you regarded it as capital or not, what information would you desire to obtain about it before giving your reply?

11. Explain the difficulties in the use of the word "Capital."

12. Describe "Capital" from the different points of view; as: production and revenue; fixed and circulating; social and individual.

13. Illustrate the bearing and importance of capital upon the production of wealth by reference to the economic conditions of—

(a) England and India.

(b) Australia in the present day and 100 years ago.

14. Draw up a simple *pro forma* balance sheet of a trader which will show at a glance: (a) The amount of capital employed in the business; (b) the amount of fixed assets; (c) the amount of floating assets; (d) the amount of floating liabilities; (e) the amount of capital owned by the trader.

15. Into what kinds of shares may the capital of a company be divided?

16. "The meaning of the word 'Capital' is not always the same. Its significance is apt to vary with the context." Explain and discuss this statement.

17. Consider briefly how a trader may obtain additional capital for a permanent expansion of his business. Would he necessarily adopt the same means if the expansion were intended only to be temporary? If not, why not?



## SECTION II—INDUSTRY

### CHAPTER VI

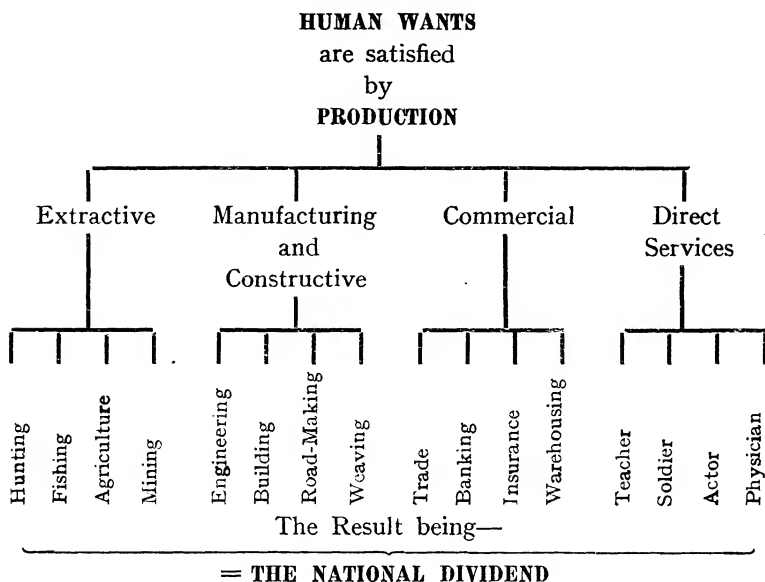
#### THE CLASSIFICATION OF OCCUPATIONS

THE first test of the economic condition of a country is its annual production of goods and services. Within recent years this aggregate national income for the United Kingdom has been estimated by several authorities at nearly £4,000 million. This means that if the rent of every landlord, the profits of every employer, the interest paid to every capitalist, and the money value of the paid labour which is earned were all added together the total would amount to this sum. To achieve this result there is required an infinite variety of labourers, all of whom are engaged in industry and are endeavouring to increase the values of materials or of services. All such persons are producers since they assist in so transforming the resources of nature as to render them suitable for the satisfaction of human wants.

At the beginning of the nineteenth century, writers on economics used the word "production" in a very narrow and erroneous sense. They classified labour as "productive" if it resulted in increasing the value of materials, and unproductive if it did not. A tailor was productive because the clothes he made were of greater value than the cloth; but many people such as soldiers, sailors, lawyers, teachers, etc., were regarded as "unproductive." Modern writers, however, consider that all these classes of the community are productive, since they increase the efficiency and save the time of the more directly productive workers. Thus, the soldier protects them from hostile invasion; the lawyer decides their disputes; the teacher improves their intellects, etc. Hence, in economics, the terms "production" and "industry" are synonymous, since they both comprise the sum total of those activities, physical or mental, which are engaged in the creation, increase or maintenance of values. This may be summed up diagrammatically as shown on the next page.

It will be seen that the desire to satisfy a human want is the





mainspring of the efforts which are put forth in the production of commodities. On account of the advantages derived from the division of labour, human effort manifests itself in a multiplicity of activities which have, in the course of time, become separated into distinct callings. The whole of these productive activities may for convenience be divided into four great divisions—Extractive, Manufacturing and Constructive, Commercial, and Direct Services.

The first two, viz. the Extractive and the Manufacturing and Constructive, are frequently classified as *Industry*.

**EXTRACTIVE OCCUPATIONS.**—These are engaged in supplying those commodities which are produced with comparatively little assistance from man, and are merely obtained in order to be used directly or are further worked up by the manufacturing industries. The separate branches of the extractive industries are to be distinguished as follows—

(a) *According to their stage of development.* From the nature of man and the course of industrial progress it follows that the raw materials which are most easily acquired form the earliest basis of economic life.

(b) *According to the degree of human co-operation with the*



*productive activity of land.* Certain branches have scarcely an occupational character and the workers are merely concerned with the collection of products already prepared for them by Nature, as in the case of hunting, fishing, mining, and the gathering in of wild fruits. Other branches of industry closely connected with Nature but in which the application of human skill is much more pronounced are agriculture, cattle-rearing, and afforestation.

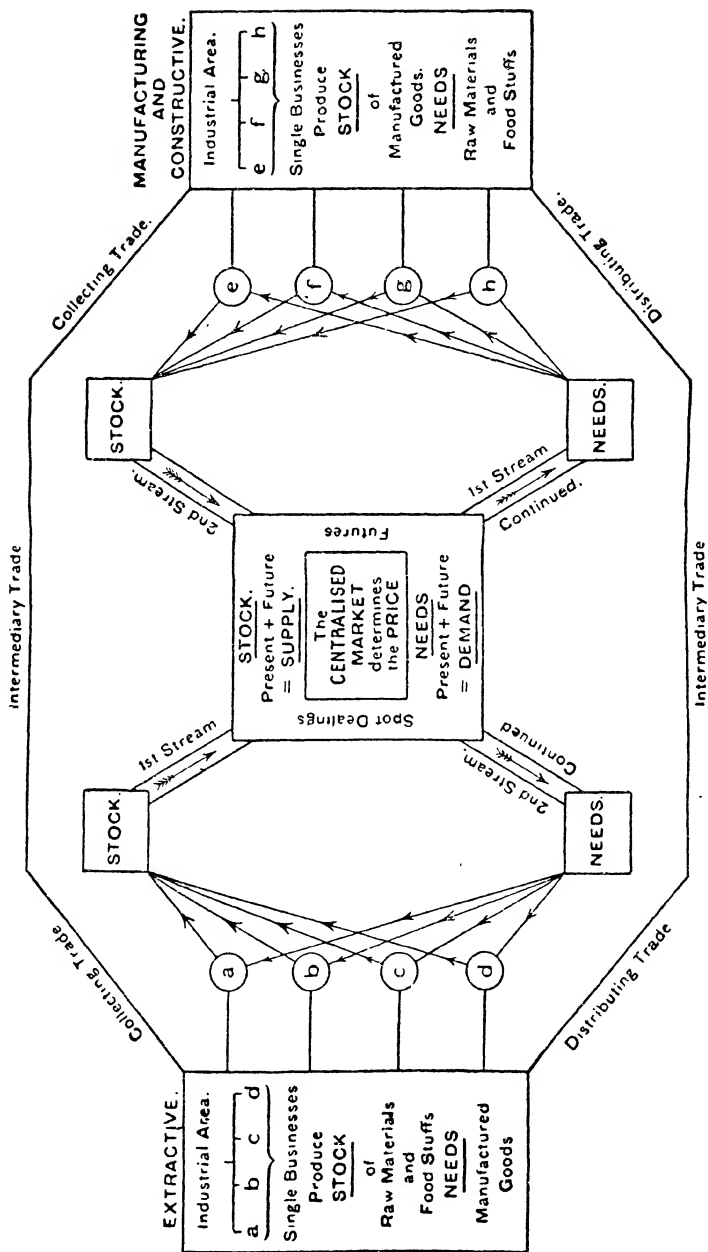
**MANUFACTURING AND CONSTRUCTIVE OCCUPATIONS.**—These consist of occupations which are concerned with the working up of raw or partly finished materials into finished articles or in putting together already existing materials. Manufacturing undertakings aim at producing a change in the raw materials, in order to increase their values, and also work mechanically the transformation of goods. Among such undertakings may be mentioned iron-works, breweries, flour mills, the making of machinery, boiler-making, china and porcelain works, weaving and spinning. As opposed to these are the constructive undertakings, which include the sinking of shafts, the laying of roads, railways, and cables, etc. These have reference to the building of, and the fitting, connecting, and completion of materials which are already prepared.

**COMMERCIAL OCCUPATIONS.**—This branch consists of all those activities which have for their object the exchange of goods between the extractor and the manufacturer, or between the manufacturer and the consumer. The function of commerce in the industrial organism is to bind together the different sections of production by procuring the exchange of their commodities according to the principles of economy. The occupations included under the heading of commerce are engaged in effecting the exchange of goods between producers and consumers, and in seeing to the transport and insurance of the goods. Commerce must, therefore, be regarded as the last link in the chain of productive activity.

**PERFORMANCE OF DIRECT SERVICES.**—This group of occupations includes all those which are engaged in increasing the efficiency and in saving the time of the more directly productive workers, but are not themselves engaged in the production of material commodities. Among such occupations are those of a protective type such as soldiers, sailors, policemen, etc. This group also includes those engaged in intellectual pursuits, such as teachers, lawyers, musicians, etc.



# THE CLASSIFICATION OF OCCUPATIONS





**INTERDEPENDENCE OF OCCUPATIONS.**—From the diagram on page 53 it will be seen that the two main feeders of the world's commerce are the extractive and manufacturing industries, which are dependent upon each other in the production and consumption of goods. In commerce, each separate business appears in a two-fold manner—in the first place, as a supplier of marketable goods and services, and, secondly, as a receiver of goods and services ; in the former case acting as a seller and in the latter as a buyer. Every business undertaking is a producer to the same extent as it is a consumer, and pays for the products it receives by supplying an equivalent amount of goods or services in exchange. Hence there exists a kind of set-off between production and consumption.

The exchange of goods between the persons engaged in the various branches of industry is only possible by the establishment of a special organisation, and it matters little whether this organisation is connected with the manufacturer or the consumer or whether it is effected by a specialised person such as a merchant.

The commercial organisation has to act as a link between the direct producer of the goods and the consumer in the fixing of the price. It fixes the payment to be made to the supplier of the goods in terms of money, and on the other hand it determines the purchasing power of the consumer. At the present time this function of determining price is fulfilled through the medium of the world market, where one merchant represents the offer of the goods on behalf of the direct producers, which is known as supply ; and another merchant represents the needs of the consumers, which is known as demand. Therefore, the price is arrived at by the competition between the agents of the producers and consumers, or by what is sometimes referred to as the " higgling of the market." The probability that future stocks are likely to be brought on to the market will tend to lower present prices just as a probable increase of future prices will tend to raise present stocks. The effect of these two streams, i.e., future demand and supply, is the production of a continual fluctuation of prices which are lowered when supply is enlarged and raised when demand is more intense, until the higgling of prices brings about a point of equilibrium through the operation of economic forces.

**Concrete Example.** An analysis of the processes whereby a woollen vest comes into one's possession will reveal the fact that we owe it



to more than one occupation that we are able to procure such an article. We may imagine that the raw wool is produced in Australia by a large number of individual farmers—*a, b, c, d* in the diagram—all of whom are engaged in an extractive industry. The wool in question once adorned the back of a sheep on the Darling Downs. The owner of the sheep had combined capital and labour and organization to set his sheep run going. Eventually after clipping time we may imagine him arranging to rail the wool to Sydney, where buyers of many nations would compete at the sales for the raw material. Our wool having been sold to a British representative, now forms part of a cargo which is transported to London, where it helps to increase the total supply received from other parts of the world. Banking facilities, insurance, warehousing and transport all play their part in ensuring that the wool shall reach the British buyer. These component parts of the great organism—commerce—are set in motion to overcome the obstacles which exist between the seller in Sydney and the buyer in London—the obstacle of place, i.e. by transport and insurance which ensures safe and speedy change of locality of the goods, and the obstacle of time, that is by warehousing in its broad sense. Arriving in London, the demand for the total supply of wool will proceed from the separate businesses engaged in wool spinning—*e, f, g, h*—in the diagram. In the determination of price, both the actual and the anticipated or future demand and supply enter into consideration. The interaction of the forces of demand and supply will determine the price of the raw wool on the London Exchange. The woollen manufacturer by bringing together the necessary factors of production is in a position to produce a cheap garment of a different type—in this case a woollen vest. As a result of the action of the law of increasing return he is able to avail himself of the advantages of large scale production. His sales department will be in close touch with a number of retailers of woollen goods and in time the raw materials received from Australia via London having been worked up into the finished article, will be dispatched to a retailer in the form of a vest. The various stages through which the wool has passed from the time of its arrival in London to that of its receipt by the retailer in the form of woollen vests have involved many economic factors, notably the granting of credit through the medium of the banking system, the transport of the goods by rail and road and the various stages of



production in the factory itself until it is finally handed over to the customer.

**EVOLUTION IN INDUSTRY.**—The relative importance of the different branches of production varies with the economic development of the country. For instance, in Ancient Britain, the inhabitants were engaged chiefly in hunting, fishing, and lumbering; in the Middle Ages, cattle and sheep-rearing became important, and this was followed by the development of wheat-growing, the importance of which reached a culminating point at the end of the eighteenth century. Since that time manufacturing and commercial occupations have become increasingly important. Such changes are constantly taking place in the life history of most nations.

## TEST PAPER VI

1. Illustrate by reference to the condition of industry in the United Kingdom whether employments can be classified as "productive" and "unproductive."

2. Into what four great divisions may the various economic activities of man be grouped?

3. Write down at random as many different occupations as possible.

4. Classify the occupations given in the answer to Question 3 according to their respective divisions.

5. Mention some finished article in which you are interested, and trace it back to the source whence it came as a raw product.

6. Mention the chief stages through which raw wool must pass before it is made into cloth.

7. Distinguish the various classes of labourers required before any article of food, such as tea or sugar, can be brought to the consumer's breakfast table.

8. "The popular distinction of industry into agriculture, manufacture, and commerce . . . fulfils very badly the purposes of a classification." (*J. S. Mill.*)

Discuss this statement, and give your own classification of industry, explaining the principle on which it is based.

9. It has been suggested that industries should be classified into "primary," "secondary," "tertiary," and so on. Apply this system of classification to the industries of the United Kingdom. Explain the basis of your system.

10. Classify the following occupations—

Butcher, soldier, carrier, tailor, analyst, barber, miner, spinner, weaver, dyer, jockey, bricklayer, dentist, rancher, and cashier.

11. Mention some of the meanings usually applied to the term "industry." Which, in your opinion, is the most useful for scientific purposes?

12. What is the distinction between "manufacturing" and "constructive" industries?

13. Discuss the difficulties met with in the attempt to classify occupations so that the groups are mutually exclusive. Give the classification which you consider to be the most satisfactory.

14. Discuss the appropriateness of the term "Producer" as applied to a farmer, a miner, an engineer, a doctor, a teacher, and a film actor.



## CHAPTER VII

### THE EXTRACTIVE INDUSTRIES

THE extractive industries are engaged in raising from the soil or obtaining from beneath the earth's surface various forms of wealth. They are essentially local in character, being largely controlled by climatic conditions. The main occupations under this branch of production are hunting, fishing, agriculture, mining and afforestation.

(1) **HUNTING.**—Formerly, hunting played an important part in the industry of the people, since it often formed the means of livelihood for whole nations and tribes. At the present time, however, it is of little importance as a separate calling, and is generally to be found combined with fishing and the production of raw materials of vegetable origin. In a hunting state, manufacture is limited to families which produce for their own use from the raw materials supplied by nature ; such as wood, bones, hides, and horn. Hunting is a primitive occupation and along with it there is to be found no class differences such as the antagonism between free-men and slaves. Moreover, very little capital is required, and this usually consists of weapons, tools, and implements. The family income is irregular, being derived from the spoils of the chase and from the abundance of wild fruits, and the transition from abject want to superfluity takes place with great abruptness. As a class, hunters amass little wealth, since their nomadic life renders the collection of stores very difficult.

In hunting, the essential condition for prosperity is the possession of grounds rich in game ; but as these can be easily exhausted, a change of settlement is not infrequent and a fight is often necessary before fresh hunting grounds can be procured. Hence among hunting peoples there is a perpetual conflict waged between the different tribes and peoples, which resembles the struggle for existence among the lower animals. In consequence, such a state is characterised by scarcity of population, and concentration in towns is impossible, so that the status and intellectual development of the people remain at the lowest level. Pure hunting races are, nowadays, very few in number, and the time when Britain consisted of hunting tribes dates back to the times of pre-Roman occupation.



When cattle-rearing, agriculture and the exchange of agricultural products begin, a gradual transition takes place from a purely hunting to that of a higher economic state. The question as to whether such transitions are possible and easy depends on the peculiarities of the people and their places of abode, or whether they are in touch with tribes in a higher state of civilisation.

In civilised countries where the population has increased enormously the forests have been reduced, implements for hunting have been improved and in consequence game is much more scanty. Hunting, therefore, finds employment for very few people, and even then only as a by-employment. The profits on the sale of meat, skins, feathers, etc., derived from the chase are small in comparison with the expense of feeding the game. Therefore, in modern civilised countries, hunting is retained merely as a form of recreation and is usually regulated and protected by law.

(2) **FISHING.**—This industry is frequently closely connected with hunting. If it is the main employment of the people, then very rich fishing grounds are required, although they are not so easily exhausted as hunting grounds. With regard to peaceful behaviour and permanence of abode, fishing peoples are superior to those of hunting, and they are generally to be found concentrated in villages and towns where social grades are more noticeable. The fishing operations are conducted by single families and sometimes by the co-operation of a number of families. The outlay and working capital is small, but a certain amount is required. The transition from fishing to agriculture and from fishing to trading takes place easily and often almost imperceptibly. At the present time, peoples engaged exclusively in fishing are to be found concentrated along specially situated coasts or districts, as in the case of the banks of Newfoundland. Among civilised peoples the following types of fishing are to be distinguished—

(1) **Fishing in Open Waters.** This may consist of high sea fisheries which, according to international law, can be conducted free at distances of three miles or more from the coast; or coastal fisheries which are to be found along the banks of rivers and sea-coasts. Fishing is very important in all countries which are rich in waters, for great stretches of water may be made to yield as much as similar areas under agriculture. The greatest yields of fish are to be obtained from high sea fisheries, although much capital and



considerable risk are involved. Fishing is the best training-ground for shipping, and in many cases, as for instance in the case of Great Britain, it has been its foundation. The quantity of fish in inland seas and rivers seems to decrease, owing to the growth of traffic and the pollution of the rivers. Fish is found in greatest abundance in countries where there is a small population and little commercial intercourse.

(ii) **Fishing in Protected Waters.** This is conducted in ponds where fish are artificially hatched. In many cases good yields are procured on very small areas. The use of fishing waters is under legal restriction, and is confined to certain seasons so as to safeguard the fish at the time of hatching. Further, as to the fish that may be caught, a minimum size is often stipulated.

(3) **AGRICULTURE.**—Agriculture produces raw materials of vegetable and animal origin. The most important products are food-stuffs, which agriculture alone can supply, so that it is regarded as a fundamental industry in any economic system. It employs the greatest number of any calling, and its extension is limited only by the extent and fertility of the soil which is capable of cultivation. Agriculture exercises a great influence on the increase of population and on the development of other branches of production. An increase of population is conditional on the extension of agriculture, and where such extension is no longer possible because the soil is already under cultivation, production can be still further continued by means of intensive cultivation. In comparison with other callings, the individual farmer has the advantage of being able to supply himself with all the necessaries of life without having recourse to exchange, and therefore in this sense he is more independent than persons engaged in other branches of industry. Economic fluctuations such as those caused by changes in demand and supply are of minor importance to him since his fixed capital remains practically the same, and his opportunities of work are most secure.

**Evolution of Agriculture.** The two most important branches of agriculture are cattle-rearing and the cultivation of the soil. Cattle-rearing is the older and may constitute the main means of subsistence for a whole people; in this case it is a step in advance of hunting and fishing. As an exclusive means of subsistence, cattle-rearing can be carried on only if the wants of the people are very simple, and if the country is in possession of such a



climate that the cultivation of fodder during winter is rendered unnecessary. Under these circumstances cattle-rearing may be carried on as the sole industry without the cultivation of the soil, although it will necessitate a continuous nomadic existence.

With the advent of cattle-rearing, the importance of capital begins to assert itself, since the herds of cattle represent capital, and thus social distinctions are created. Those who have no herds are obliged to render services to the owners of the capital, so that there arise the economic distinctions between masters and workmen or freemen and slaves. Here we have also the sowing of the seed for the formation of States, and the germs of a communal interest. The production of manufactured goods is restricted to the simplest articles and is limited to the members of the family, whilst trade has not developed beyond the stage of simple barter. Any rapid increase of population is restricted by the yield of the pastures, so that no great concentration takes place. In consequence of the nomadic life of the people, their dwellings are of the rudest kind, and the whole of their property is of a movable nature. Such people may remain in the same stage of civilisation for a very long period.

Along with cattle-rearing we find the beginnings of the cultivation of the soil, small patches being cultivated at first with such plants as can quickly be harvested. Finding by experience that the combination of cattle-rearing with the cultivation of the soil is more profitable, the population gradually realise the advantage of settling permanently in the same place, and so become an agricultural people. This development, which may also arise out of hunting and fishing, is a great step in industrial progress. Production becomes more independent of nature, and economic considerations lead to an increase in the products of the soil. The laws of utility are made to supersede the free operations of nature, so that by cultivating the soil in a better manner it is possible to feed a larger number of people from the same area. Human wants tend to become more varied and are satisfied by regular and peaceful work.

When permanent settlement is assured, the people begin to erect more substantial dwellings, which give a higher standard of comfort. Step by step communities are formed and order is established, and among the people living together as neighbours there grows up a permanent bond of interest which slowly develops into a State.



Interest in the soil forms a basis for the ownership of land, the legal conditions and stipulations differing among different peoples. At first the land system is based on communal ownership, together with certain individual rights of use for the members of the community. Later on portions of such property pass into the hands of individuals and are privately owned.

A permanent abode leads to a feeling of home life and to a sense of common interest. With the beginning of agricultural life, large gaps exist between the different settlements which are used solely for hunting or for cattle-rearing. With the increase of population larger areas are brought under the plough: at first, the more fertile lands, and then the less fertile, being cultivated.

The demand for manufactured articles is met by the agricultural people themselves, who produce articles of a similar kind, and out of this there gradually develop separate manufacturing industries which are at first based on the treatment of metals.

**ECONOMIC FACTORS.—Land.** Since agriculture is so largely dependent on the nature of the soil, land is the most important factor for the successful conduct of that industry. The soil feeds and nourishes plants and animals, and on its fertility depends its productive potentiality. In case the yield becomes diminished, however, it may often be restored by the application of fertilisers. In addition to the extent and fertility of the soil, climate plays an important part, although this can be little influenced by human foresight and labour.

**Labour.** Next to land, labour is the most important agent in agricultural production. The further agriculture progresses, the greater are the efforts which are made to guide the productive powers of the soil, and to maintain their fertility. The most necessary work in agriculture is of a simple kind and can easily be adapted to natural and seasonal changes. The agricultural labourer has, therefore, to change his work with the seasons, so that an extensive division of labour is rendered impossible. Agricultural work is more healthy than that of most other callings, and the physical and mental activity involved in its conduct prevents the workers from becoming over-specialised or one-sided.

Agricultural labourers are engaged either permanently or at a fixed daily wage. Daily labourers are frequently in possession of their own farms or holdings, and are generally in a fairly good



position. Machinery enters into agriculture but slowly, and the bad consequences which attend its introduction into manufactures are seldom seen in agriculture.

**Capital.** With the increased development of agriculture, capital takes a more and more important place. In addition to buildings, the *fixed capital* also includes machinery and implements, the rolling stock, and animals used for breeding purposes. Among the items of working capital are food-stuffs, corn for breeding purposes, corn for seeds, fertilisers, etc. The *working capital* usually amounts to about 40 per cent of the total capital invested.

**Organisation.** The method of organisation is dependent on the soil and climate, on the available supply of labour, and on the conditions of sale. In the first place, soil and climate have to determine whether the main basis of the business shall be the cultivation of the soil or the rearing of cattle, whilst the conditions of sale determine the proportion of the different factors engaged in production. In this respect, the difference of extensive and intensive agriculture is of importance. If a large area of land is cultivated very lightly and without much preparation or expenditure, cultivation is said to be extensive, whereas intensive cultivation is the thorough and careful treatment usually of a small area. In extensive agriculture the capital is of less importance, the production being left chiefly to the free operation of nature. Great stretches of land are worked with comparatively little labour and practically are not fertilised at all. After the harvest, the land is allowed to remain fallow in order that it may recover. Extensive cultivation is necessary where the population is small, manufactures undeveloped, trade inconsiderable, and the demand for the products of the soil very limited. Under such circumstances, natural economy often prevails, the individual farmer producing only what is required by his own household.

In intensive cultivation, however, capital and labour are so applied to the soil as to produce the largest possible yield. The soil is carefully drained or watered, as the case may be, and fertilisers are freely used to render the area more productive. This system is only possible, however, where there is a great demand for agricultural products, and exists chiefly in progressive states of civilisation, and especially in the neighbourhood of towns.

**Small Holdings.** A distinction must be made between small,



medium, and large holdings, although it is impossible to draw a clear line of demarcation. Very small holdings do not employ any ploughing team, whereas the medium holding would employ one or two, although, as in the small holding, the farmer will assist personally in the manual work. In the case of large holdings, one or more managers may assist in the direction of the whole concern.

Small holdings possess the advantage that the farmer can devote his attention to such marketable vegetables and plants as require much diligence and careful treatment of the soil. If the land is divided into small holdings, larger gross and net yields may be obtained from the same area than if it were worked on the system of large holdings. The holding of the small farmer is continuously under his own eyes, and he can employ his wife and children to assist in the work, so that he is not dependent on outside labourers. Sometimes, however, the small holdings fail to offer sufficient scope for the abilities of the farmer, and the advantages of division of labour and the utilisation of the best machinery are absent. Further, in the case of a bad harvest, the whole undertaking is endangered.

Such small farming is most successfully carried on in the vicinity of towns where such products as garden plants, milk, dairy products, fruits, etc., can be easily marketed.

The prospects of the small farmer are more secure when access can be had to profitable by-employment in times of agricultural depression: but where such opportunities do not exist, small farming is a very risky enterprise on which to embark.

**Large Holdings.** Farming on a large scale has the advantages of comparatively small working expenses, a better division of labour, the employment of superior machinery, and the possibility of extensive improvements in the soil by means of irrigation or drainage, and other technical improvements. Such advantages, however, are only possible where capital, intelligence, and diligence are sufficient. The disadvantage of large-scale farming is the great social clearance which is usually created among the agricultural population. The establishment of large holdings leads to the disappearance of the independent yeoman class which is often replaced by a rustic labouring proletariat. The value of the gross and net yields of large holdings is comparatively small, owing to



the fact that the land cannot be exploited to the same extent as with small holdings.

**Medium Holdings.** The medium-sized holdings come between the above-named extremes, and these also have their advantages and disadvantages. The ideal seems to be that these farms should predominate and that the small farms should only extend where they are justified from an economic standpoint, and large holdings should be developed to such an extent as will allow for technical progress to be made.

If the establishment of large holdings is carried too far, it is at least as detrimental as the too minute subdivision of the land.

**Systems of Working.** As the main branches of agriculture, such as cattle-rearing and the cultivation of the soil, as well as the use of the land for pastures and meadows, may be carried on together, it follows that a great variety of systems for working the land may be distinguished, in which the distribution of the fields differs considerably according to the capital outlay and the yield expected. The choice of the right system depends on the nature of the soil, the extent of capital, and the prevailing price of the produce. These different systems are to be distinguished by the method of crop rotation. Three main systems may be mentioned—

(a) **SYSTEM OF GRASS CULTIVATION.** Under this system the land is cultivated with crops for a number of years and is then used again as meadow land. It is a rude economical form, in so far that only a small portion of the whole area is under cultivation, and the remaining area is used as meadow. It is sometimes known as the system of Meadow Culture.

(b) **CORN SYSTEM.** According to this system, the greater part of the area is under corn whilst the remainder lies fallow or is grown with other crops. Frequently this system of corn cultivation is carried out as a three-field system, viz., the area of each farm is divided into three parts—one is sown with winter corn, one with summer corn, and the third is left fallow.

(c) **CHANGE OF CROP SYSTEM.** According to this system the whole of the soil is cultivated every year, but the crops are changed. This is a most intensive exploitation of the soil, requiring the most careful treatment and an extensive use of fertilisers. It is frequent in countries which are densely populated. By-employments may also be successfully carried on alongside the main agricultural work



as in the case of the distillation of spirits, breweries, dairies, the milling of flour, and the production of sugar. The proximity of such manufacturing industries reflects a certain beneficial influence on agriculture itself.

**Forms of Tenure.** The chief forms of land tenure are as follows—

(a) **SOLE MANAGEMENT BY THE LANDOWNER.** This is the most desirable form from the economic and owner's standpoint, for it ensures regularity in the yield and improvement of the soil, and affords the greatest continuity of employment and satisfaction both to the owner and to the labourers.

(b) **ADMINISTRATION BY PAID MANAGERS.** This system is usual only in the case of very large holdings. The managers have often no very great interest in the continuous success of the undertaking and are difficult to control, so that the net profits due to the owners are not very large.

(c) **TENANT FARMING.** Under this system, which is usual in England, the land is owned by the landlord and let out by him at a rent to tenants, who work it with the aid of hired labour and, perhaps, borrowed capital. The interests of the owner and of the tenant are not identical, for the tenant aims at quick returns and not at permanent yields or improvements of the soil. Larger tracks of land are occupied by cultivators who pay for the use of the land in other ways than by a fixed money rent. Among these may be mentioned—

(1) *Metayage*. Here the landlord provides the land and the bulk of the capital; the cultivator provides small working implements, and hands over to the landlord a customary proportion of the produce, usually a half. This system is supposed to give both the landlord and the tenant a decided interest in making the produce as large as possible, so that a wise landlord will assist a good tenant by providing fixed assets and by advancing capital on easy terms. The system is very usual in Italy, Portugal, and France.

(2) *Ryot Tenure*. Under this system the cultivator is the owner of the land, subject to the payment of a proportion of the produce to the Government. Such a rent is much the same as a land tax. The assessment is usually made for thirty years. It is common in Bombay, Madras, and Burmah.

(3) *Cottier Tenure*. The word "cottier" originally meant a



sub-tenant who rented a cottage and an acre or two of land from a small farmer. The system was introduced into Ireland in the seventeenth century, when the land was let by the Irish landlords in small plots to peasants who cultivated it with their own labour.

The term has gradually come to include all peasant farmers.

**Agricultural Output.** The gross output of an agricultural undertaking consists of the total yield of its products, an exact calculation of which is rendered difficult owing to the fact that portions of the produce are continually being sold, whilst others—such as fodder, fertilisers, wages paid in food-stuffs, etc.—are used in the conduct of the industry. Again, a portion of the produce is used by the farmer for the upkeep of his family. In estimating the gross output, the final product only must be calculated. It is impossible to state with exactness the gross production of agriculture for the whole country, although a rough estimate is now supplied by the census of production.

After deducting the expenses of production, the net result is determined. The expenses of agricultural production consist of wages, repairs, and depreciation of buildings, farm utensils, and rolling-stock, the cost of seeds, fertilisers and fodder, as well as the expense of insurance, etc. After deducting these items, the net amount comprises the items for ground rent, interest on capital, wages, and the owner's profit. The amount of net profit from year to year is difficult to calculate, although it is necessary for the purpose of estimating the capital value, the fixing of mortgage loans, and the assessment of rates and taxes.

**Agricultural Credit.** The more intensively cultivation is carried out, the more important does credit become in agriculture. Farmers rarely appear as creditors, for they usually sell their products for ready cash. They more frequently appear as debtors, accepting credit for the purchase of real estate rather than for personal use.

**CREDIT ON REAL ESTATE.** This kind of credit is used by the farmer to enable him to pay out co-inheritors so as to avoid the necessity of paying the whole of the purchase price at the time of the purchase. It is also used for the purpose of effecting improvements on new buildings. In all these cases the credit facilitates production, and in case of withdrawal of loan it is necessary that notice be given so that the redemption may take place gradually.



By mortgaging his fixed assets the owner can offer a good security to his creditors, so that he is required to pay a smaller rate of interest than would be the case with personal credit. In order to meet the demand for credit on real estate, agricultural credit associations, banks, etc., have been founded, and make advances. The chief points to be observed in regard to the arrangement of a loan on real estate are the correct calculation of the period of indebtedness, reasonable limitation of the interest, and sum of money lent, as well as the charges made for effecting the loan.

**PERSONAL CREDIT.** Farmers should avail themselves of personal credit only when they carry on their cultivation in an intensive manner, and then for the purpose of buying fodder, fertilisers, etc., or for increasing generally their working capital. In the case of such a loan, a period of at least one year should be allowed for repayment, or according to the turn-over of the capital. If capital is borrowed for the purpose of rearing live-stock, the time of notice should be still longer. In most cases private loans are detrimental to the interests of the farmer in consequence of the uncertain conditions appertaining to interest and redemption. For farmers the special credit associations, which are generally limited to the locality, are more suitable for the obtaining of advances and of credit. In this respect the Raiffeisen associations are worthy of mention. These associations, which are named after their founder, have made remarkable progress in Germany in the form of mutual credit societies among farmers. These farmers lend money to each other through the medium of their societies, and employ their collective credit to obtain loans from outsiders upon terms much more favourable than any individual would be likely to receive for himself.

**Co-operative Banks and other Associations.** In Anglo-Saxon times, and for centuries later, the cultivation of meadows, pastures, and stretches of forest land was carried on by the villagers, who held rights in common over the land. This system was very wasteful and hindered the introduction of improved methods of cultivation, so that in many of the village communities a transition from common ownership to private ownership was considered as a progressive step. In the case of the forests alone was co-operative use regarded as being advantageous. The requirements of the present day have led to the formation of local



co-operative associations for the purpose of equalising the economic drawbacks of small holdings in competition with large ones. Such new co-operative associations are in the first place societies for the amelioration of agriculture by means of the carrying out of drainage schemes, irrigation, and the cultivation of forests and moors. There are also co-operative credit societies for the procuring of working capital in the form of agricultural machines, etc. ; and societies for the preparation of commodities (e.g. co-operative dairies).

AGRICULTURAL SOCIETIES comprise larger areas than the agricultural banks, and their function is to extend agricultural knowledge and experience, to improve matters technically, to conduct experiments, to arrange conferences on agricultural subjects, and to represent the agricultural interest in contrast with that of other industries.

Finally, there are Co-operative Societies engaged in the *Sale of Agricultural Produce*. A sketch of the development of this form of co-operation during the past half-century is contained in a report on the "Co-operative Marketing of Agricultural Produce in England and Wales," published in 1925 by the Ministry of Agriculture. According to this Report the essential principle which distinguishes co-operative trading, as exemplified in Denmark and other countries where it has proved successful, lies in the fact that co-operation involves the idea of joint action by all the members for mutual benefit, that is to say, it is the banding together of producers for the collective sale of their combined produce. The success of such a Society depends upon the support of its members. If it does not receive that support and has to conduct its business on the same lines as a joint-stock company it has no essential advantage in competition with private traders or companies. Failure to appreciate this point is perhaps the most striking characteristic of co-operative trading in Agricultural Produce in this country. Producers have joined these co-operative societies and have subscribed a certain amount of capital but, broadly speaking, there has been little realisation of the necessity for supporting the societies they have formed. It is not too much to say that to this source can be traced the majority of the troubles of co-operative societies in Great Britain.

Where co-operation is worked on sound principles and under



good management it gives the producer the opportunity of securing on the average the maximum return for his produce ; this result, however, cannot be obtained without the application of proper business methods, and in this respect the following points are important—

(1) A society needs to be on a sufficiently large scale to justify the employment of an efficient manager at a fair salary. It needs an assured prospect of sufficient business to enable it to operate with overhead charges at least as low as those of any corresponding private business.

(2) To ensure this sufficient volume of business, the members should each definitely contract to supply a certain agreed quantity and should recognize a liability for penalties for failure to fulfil the contract.

(3) To guard against possible loss from fluctuating prices the members should agree to accept payment on account for goods until the actual cash receipts are known, and to a division of the surplus in proportion to the goods supplied.

Given reasonably good management, a society established on these lines should be able to secure for its members larger returns on the average than would be obtained by individual sale, with little risk of loss of capital.

(4) **AFFORESTATION.—Object.** The cultivation of forests has for its object the supply of timber for household purposes, for building and manufacturing, and the preservation of forest areas which are of importance in regulating the climate and the flow of the rivers. The significance of afforestation in the national economy is seen in the large number of products which result therefrom, and also in rendering useful large stretches of land which would otherwise be of little or no value.

**Factors of Production.** Land is by far the most important factor in afforestation, whereas the part played by labour is comparatively unimportant.

In afforestation the capital consists of the forests themselves and the character of their timber. Under the powerful influence of nature, this considerable capital value gradually reproduces itself with the employment of a very small amount of labour. A characteristic feature of this branch of industry is its failure to succeed if undertaken on a small scale ; therefore it must be carried out



over a large area, so that it is more suitable for State or municipal enterprise.

**Administration.** If it is intended to carry on the production of timber continuously without a decrease of the capital value of the forests, it is important that the amount cut should not exceed the annual increase of the timber. Hence it is necessary that a careful estimate should be made with regard to the existing timber reserves and the annual rate of growth of the timber. The rate of growth in cubic measurement as well as in timber value differs with the various kinds of wood, since it depends on the species of the timber as well as on the nature of the soil.

**Forms of Exploitation.** The methods of exploitation may be classified as follows—

(1) The exploitation of *high forests* in which the trees are permitted to grow as tall as possible, and are cut down only after a long period of time.

(2) The exploitation of *low forests* in which the natural growth of the trees is interrupted by the removal of parts of the trees for special purposes.

(3) The exploitation of *medium forests* in which low trees are grown alongside tall ones.

In some cases the quantity of timber grown on a certain area is the important consideration, whilst in others it is the value of the timber.

**The Yield of Timber.** The yield consists, in the first place, of the increase which has occurred in the forest itself, together with the amount of timber collected in making roads through the forest; and in the second place, in the production of bye-products, such as resin, grass, etc. The prices of timber are the lowest where there is the greatest superfluity. An important point in afforestation is the existence of good transport facilities. With regard to the maintenance of the yield the following policy should be adopted—

(a) A certain area should be set aside by the State for the purpose of afforestation, and efficient managers should be appointed to carry on the work.

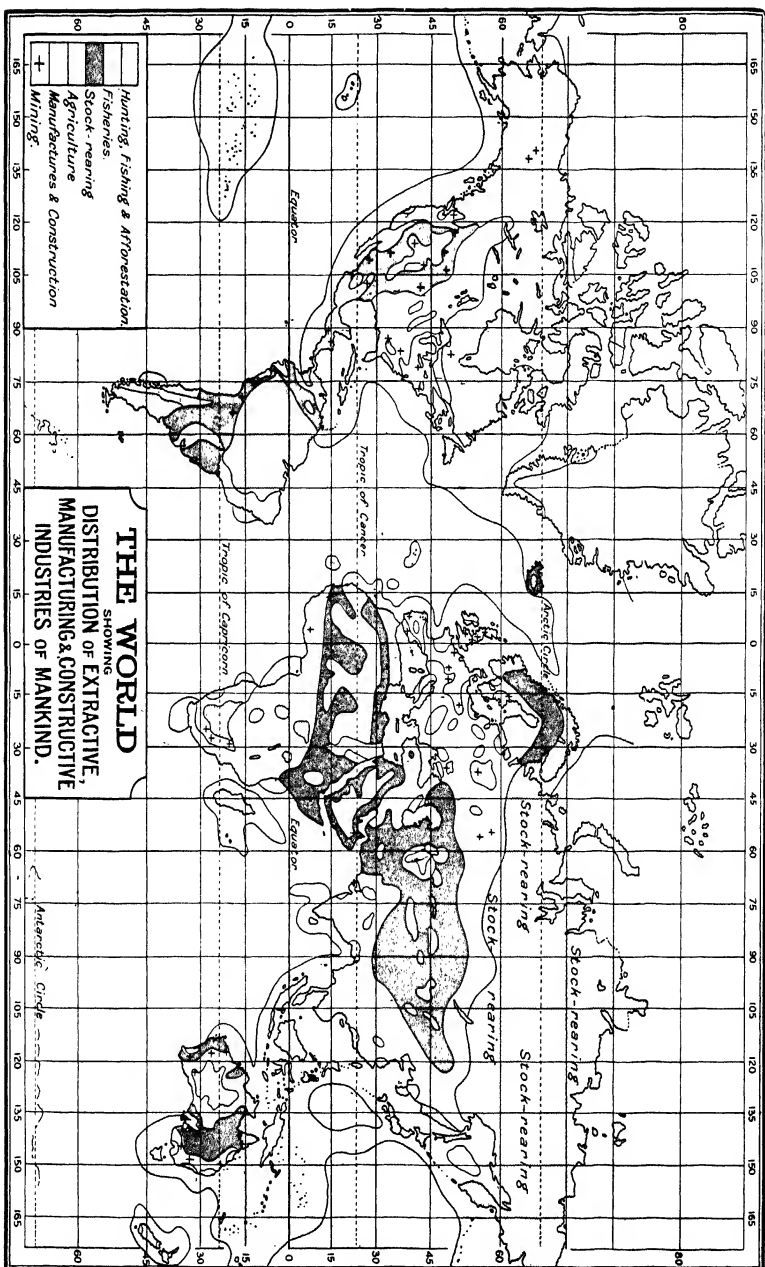
(b) If necessary, assistance should be given by the State to municipalities for the conduct of afforestation.

(c) Legal protection should be offered to prevent wilful damage to forests.















In most civilised countries replanting is rendered obligatory on all persons engaged in removing the trees.

(5) **MINING.—Natural Conditions.** Mining is more dependent on nature than any other branch of industry. Nature is the determining factor, for mining is impossible if there are no natural mineral resources. Hence this branch of production is usually strictly localised and the minerals when once removed cannot again be replaced. In the distribution of mineral deposits over the earth's surface, nature has been very fickle so that the results of the working in different areas vary considerably.

**Labour.** Mining is one of the most arduous occupations, and is at the same time subject to peculiar dangers. In this calling the labourer has little, if any, prospect of becoming his own master, and must, therefore, work for a wage. The workmen generally live in the vicinity of the mines, since they expect to be permanently engaged in mining work, and it rarely happens that there is any great influx of labourers from other callings. If the mines are prosperous, the wages may be high, but if depression sets in, it is difficult for the miners to find other kinds of work. Owing to the fact that the workers are almost exclusively dependent on mining, a state of trade depression often causes great hardship in mining districts.

**Capital.** Fixed capital plays a very important part in mining and assumes the form of shafts, galleries, machinery, etc., which cannot be removed without considerable loss. In no other branch of industry are there such large amounts of capital risked at the same time. Therefore mining is less suitable for ownership by a single person than for companies possessing large capital.

**Output.** Mining differs very greatly from most other industrial enterprises by its entire dependence on nature for the result of its working and the extent of its deposits, for these can be altered neither by the progress in technique nor by the investment of capital.

The rent of mines differs from that of land in that it is liable to complete and speedy exhaustion, and varies with the value of the mineral products and their cost of production. In consequence of the fluctuation in the rent of mines, the purchase consideration is very difficult to ascertain, as is the working period, except in the case of coal-mines. The duration of the working period varies



considerably. Tin mines, for instance, in some places have been worked for hundreds of years, whereas oil wells are generally exhausted in from two to ten years. In the case of coal, it frequently happens that mines have to be closed because they are incapable of withstanding the competition of richer deposits, and the considerable capital invested in the mines does not at first yield any interest and is lost entirely if there is no prospect of further yields.

The working of coal-mines is influenced by fluctuations in the rate of wages, by alterations in the cost of transport, and by competition on the part of other mines. Although coal is essential for household, manufacturing and other purposes, and is very widely consumed, yet the demand for it is not always regular. In all mines, the cost of production increases the deeper the mines have been sunk. Reductions in the cost of transportation may be effected by means of technical progress and improvements. More than in most other industries accidents and other disasters, such as explosions and the entrance of water into the mines, often disturb the continuity of employment and the success of such undertakings.

### TEST PAPER VII

1. Enumerate the main branches of the Extractive industries.
2. Say what you know of hunting as an occupation, and mention the branch of production to which it is most closely allied.
3. What are the essential conditions for the success of "hunting" and "fishing"?
4. Why is "agriculture" regarded as a fundamental industry in any economic system?
5. Trace the evolution of agriculture.
6. What are the most important requisites for the successful conduct of the agricultural industry?
7. Compare the relative advantages of small, medium, and large holdings.
8. Distinguish, according to crop rotation, the various systems of working in agriculture.
9. What are the principal forms of land tenure?
10. Explain the object of Raiffeisen associations.
11. Distinguish between "co-operative banks" and "Agricultural Societies," and describe the function of each.
12. Enumerate the most important factors in afforestation. Why does the State usually undertake this branch of production?
13. Examine the economic characteristics of the mining industries.
14. "Mining is more dependent on Nature than any other branch of industry." Explain this statement.
15. Why are mining concerns less suitable than agricultural undertakings for ownership by a single person?



## CHAPTER VIII

### MANUFACTURING AND CONSTRUCTIVE INDUSTRIES

**NATURE AND DEFINITION.**—The second great branch of industry viz. the manufacturing and constructive industry, will now be considered. Manufacturing industries are those which are engaged in working up raw materials with the object of producing from them goods of a higher value, by processes of separation, combination, or of transformation. In a narrow sense, large scale undertakings only are called manufacturing, in contrast with the smaller concerns.

The term “manufacturing,” in the wider sense, embraces all those undertakings of a technical character which are engaged in the combination of raw materials, whether mechanically or chemically, in contrast with commerce and direct services, into which technical activity does not enter.

Historically, the manufacturing industry is younger than that of extraction. It started in the production at home of articles for the use of the family itself, and gradually, with the recognition of the advantages of division of labour, special callings were established, and became more and more numerous. From the economic standpoint, manufacturing industries are very important, because they aim at increasing the value and variety of the nation's products ; and by enabling a concentration of population to take place in towns, they offer many social inducements, such as the stimulation of intellectual life. They also exercise a favourable effect on the extractive industries by creating a demand for further products and in supplying them with tools, machinery, etc. Further, they stimulate international trade, which leads to a higher standard of comfort and intellectual intercourse among the nations.

The development of manufacturing industries along with the production of raw materials is a natural step in the progress of division of labour. The extent of manufacturing in comparison with other branches of production, varies considerably in different countries, as well as in different parts of the same country.

Manufacturing is intimately connected with the production of raw materials, because it is engaged in working up the raw products,



and the workers in the manufacturing industries are fed by the food-stuffs derived from the extractive industries.

Moreover, the market for manufactured goods is found, to a great extent, among the producers of raw materials at home. Of course, with the development of a more highly specialised system of manufactures, it happens more and more frequently that the home manufacturers have to rely on imports of raw materials from abroad, where they also find important markets for their finished goods. With the rapid development of commercial intercourse during the nineteenth century, the manufacturing industries have made great strides, population has increased, and international division of labour has led to the exchange on a large scale of manufactured products for the raw materials and food-stuffs of foreign countries. The consequence of these changes has been the increasing severity of trade fluctuations, which can only be minimised where there are good means of communication. Countries which suffer the most from such disturbances are generally mountainous districts, which are removed from the main commercial highways.

**CHARACTERISTICS OF MODERN MANUFACTURES.**—The manufacturing industry of the Middle Ages differs so considerably from that of the present time that the transition from one to the other has been called the “Industrial Revolution.” That revolution was characterised by great alterations in production, in the method of transport, and in the conditions of sale. With the introduction of machinery, production has become concerned with the output of masses of goods and not merely of separate articles. The chief inventions which paved the way to such large scale production did away more and more with the necessity for monotonous and arduous toil, which were inseparable from the use of hand labour. The production of huge masses of articles coincides with the sale in large quantities, which was facilitated by the improvements in the means of transport, by the abolition of restrictions on personal liberty, and by the better feeling prevailing among the nations, all of which helped to transform the entire globe into a great area consuming the products from its different parts.

In the industrial world of to-day there is a continuous fluctuation in the level of prices, and a constant cycle between periods of adversity and of depression. Such changes occur in almost all types of



industry, and in the majority of business houses a point of maximum and minimum activity can be distinguished.

**RELATION BETWEEN EXTRACTIVE AND MANUFACTURING INDUSTRIES.**—The primary stage of production is that in which manufacturing is carried on in conjunction with the extraction of raw materials. This often occurs where the raw materials constitute a very important part of the finished article, and where the cost of transport of the raw materials and the general expenses of the sale may thereby be saved, and thus permit of an increase of the net profit. Sometimes manufacturing processes are connected with those of agriculture, because the agricultural products can be utilised as the basis of the manufacturing industry, as in the distillation of spirits or the manufacture of cheese. The cause of the establishment of such manufactures is closely connected with the production of the raw materials. Manufacturing operations are also carried on along with afforestation, as in the case of saw-mills, charcoal, and tar factories. In these cases, the economic reason is the ability to surmount the high costs of transport by separating on the spot the most valuable parts of the raw material from those of lesser value. For similar reasons, ironworks are connected with mines, and lime-burning with the breaking of stones.

The production of raw materials is subordinate to that of manufacturing in other cases, as in china and glass factories, sugar refineries, etc. The manufacturing processes can be carried on more successfully if the raw material is in the immediate vicinity and is produced by the manufacturer himself. Another type of connection between the manufacturing and extractive industries is where there is no definite affinity existing, but the manufacturing is undertaken for the purpose of filling up the spare time of the men. With regard to the quality and quantity of work done such connection leaves much to be desired. Work which is done merely with the object of filling up the spare time of the labourer is generally very imperfectly executed, and reminds one of the primary state of all manufactures. Here the worker has neither sufficient capital nor inducement to buy good implements. Such businesses are small, and the advantages of division of labour and of improved organisation are non-existent. Moreover, labourers who have been trained for agricultural work are usually unsuitable for that of manufactures.



**ESSENTIALS OF SUCCESSFUL MANUFACTURE.**—The manufacturing industry of a nation, as a whole, as well as of each separate branch, is dependent for its prosperity on certain essentials. These essential conditions are partly natural and partly historical, although it is often possible to make them more favourable by human assistance. The relative importance of these different conditions varies at different periods, so that their influence is reflected on the existing state of industry. Every *entrepreneur* must know these conditions and influences as far as they affect his particular line of business. The main essentials of successful manufacture are to be found in the following factors—

1. Raw Materials ;
2. Labour ;
3. Capital ;
4. Conditions of Sale.

**Raw Materials.** An essential condition for the success of a manufacturing concern is the possession of abundant supplies of raw material. Under the domestic system, where the work is limited to the family, the raw materials, which are of a simple kind, are procured from the immediate vicinity. With the development of economic life, there takes place a separation between the production of raw materials and that of manufactures, so that some branches of manufacture are removed to places of consumption, whereas others remain in such places as are within easy reach of the raw materials. For instance, those manufactures are naturally to be situated in proximity to the raw materials, in which the raw product plays a specially important part as compared with labour and capital, or in which the raw materials are heavy and require large expenses of transport. Again, the treatment of ordinary metals is for the same reasons restricted to the neighbourhood of the ore and the coal-mines. In the case of better-class castings, the manufacture of machinery and the later stages of production, the works may be situated at a greater distance from the source of raw materials, since their value will stand the cost of transport.

The more developed a manufacturing concern becomes, the more easily will it flourish independently of the local supplies of raw material. The foundation of a manufacturing industry may have been due originally to the existence of large supplies of raw material, but its continuance in that particular district may be due to other



reasons. For instance, in the course of time a considerable amount of capital may have been invested in the form of buildings, technical appliances, the acquirement of a large circle of customers, and the consequent increase of goodwill ; and these may turn out to be more important than the former advantage of the possession of an abundance of raw materials.

Those branches of manufacture which are engaged in the working up of raw materials from abroad are often conducted more successfully in the neighbourhood of large seaports, where the raw material can be bought by the manufacturer himself, thus saving the agent's commissions and at the same time affording him a greater variety of choice and more frequent opportunities of profiting by low prices (e.g. by the purchase of raw materials which have been partly damaged). Further, a business conducted under these circumstances has the advantages of comparatively small expenses of transport with regard to the waste products, for these would be heavy if the raw materials had to be sent long distances. For this reason, sugar refineries have been established at Bristol and London, as well as at Hamburg, Bordeaux, and Marseilles. Other examples are the tobacco factories at Bristol, as well as cotton-spinning in the neighbourhood of Liverpool and Glasgow, these ports being very favourably situated for the import of raw materials from the United States.

Many waste materials, resulting from the consumption of a large population, are supplied by the great cities, where there is a variety of skilled labourers and a large supply of capital. The treatment of various metals, because of its luxurious nature, is carried on mainly in the great cities, where there is a demand for artistic and tasteful work. For the same reason, musical, scientific, and other instruments, as well as fine machinery, are usually manufactured in large cities.

**Labour.** One of the main points in manufactures is that there should be sufficient labour available for the different requirements which have to be taken into consideration. It is to the interest of the entrepreneurs, as well as to the workpeople, that labour should be efficient, skilful, and reliable. In the price to be paid for labour, however, the interests of the entrepreneurs and those of the workers come into conflict.

The labour engaged in manufacturing differs from that of the



extractive and commercial callings in some respects. In the extractive industries, the work consists in loosening the material resources of Nature from their natural positions, as in the case of mining, or the mere direction of natural forces into channels whereby new materials may be produced, as in the case of agriculture and afforestation.

Natural forces or powers are also used in manufactures ; but in this case they are so completely controlled that their result can be calculated exactly, whereas in the extractive industries the output is largely dependent on the fickleness of Nature. The most scientific agriculturist cannot foresee the state of the weather for the coming year, and the most careful planning of forests cannot prevent the occurrence of storms. Since manufacture is not dependent on Nature to such an extent as are the extractive industries, a more independent line of development can often be followed. Manufacturers are not bound to any particular spot, for, unlike agriculturalists, they are not dependent on the nature of the soil. The emancipation of manufactures from a particular spot, however, does not obviate the necessity for the choice of the most favourable conditions. The possibility of the establishment of an extensive division of labour dependent on local conditions is important in this respect. Again, manufactures are not so restricted in the disposal of time or by the change of seasons as in the case of the extractive occupations.

Agriculture and afforestation have to be planned according to the rotation of the seasons, but, with certain exceptions, this is not the case with regard to manufactures. The manufacturing industries remove mankind more and more from Nature, and with the increasing specialisation there is a tendency for such work to become more monotonous. Moreover, it is generally considered that there is more worry connected with manufactures than with any other kind of production.

**Capital.** One of the most important conditions of successful manufacture is the existence of available supplies of capital in the immediate locality in which the industry is carried on. In such cases, the capital is usually the result of the gradual accumulation of savings by the people, as in the case of the Lancashire cotton industry. The capital required may also be obtained by means of credit, but this is exceptional, except where the investors are



guaranteed against all risks and where there is a likelihood of a profitable continuation of the enterprise to which they grant their loans. If it is seen that the manufacturers in a certain district can produce a good return to capital invested with them, and that they can redeem with interest loans which are made to them, then in all probability a stream of capital will tend to flow to that district, so that new enterprises will be started and old ones will be revived.

Districts with a sparse population have frequently an insufficient number of workers and inadequate capital for the successful carrying on of manufactures, and are, therefore, hesitant in embarking on such enterprises. Where the climate is suitable, opportunities are frequently afforded for the production of raw materials, and this is more in accordance with the existing economic conditions than an industry which is stimulated solely by artificial means. If good means of transport are available, the conveyance of raw materials to places abroad will naturally lead to an increase of capital. Manufactured products are often more profitably imported from abroad until the time arrives when, with the saving of capital, the increase of population, and progress in technique, those branches of industry which are most in accord with local conditions, will begin to flourish and gradually supplant the demand for the imported goods.

**Conditions of Sale.** Ready access to markets, home or foreign, helps to determine the size of industries and localises them. The markets for complex manufactured articles are limited to the more progressive areas so that industries producing such articles tend to be located near the main markets where facilities for selling them exist. Manufacturing industries also require extensive transport facilities both for the raw materials which they employ and for the disposal of their finished products. Hence industries tend to grow where these facilities exist and where transport costs are low. If a manufacturing concern is to be established, a place of business should be chosen which is in the neighbourhood of such places as offer good opportunities of sale. Manufacturers of fine articles involving artistic design are more favourably conducted in the great centres of consumption. Country people desiring fancy goods prefer to make their purchases in the large towns, where a greater choice is to be obtained, and hence there is a tendency for the production



of such articles to be located there. The manufacture of fancy goods is not carried on to any great extent in the small towns, and the same difference which exists between the town and the country and between large and small towns is also found to exist between the various parts of a great city. Shops for the sale of fine articles are usually to be found in the most fashionable streets, in the vicinity of the royal residences, the theatres, and the large hotels, e.g. the West End of London. The shops for the sale of other manufactured articles are, for practical purposes, situated in the neighbourhood of the commercial or manufacturing quarters or in the suburbs. The rent of the shops situated in the fashionable quarters cannot easily be borne by articles of ordinary consumption, and, moreover, the demand for such articles is not so great there as elsewhere.

**Other Factors.**—From the foregoing it will be seen that the factors determining the success of modern manufactures are numerous and complex, since account must be taken of a great variety of natural factors—physical, geological, and climatic. Of equal importance are the economic and psychological factors. The latter may take the form of governmental or municipal “protection” of an industry in a particular locality, e.g. the special attempts made in medieval times to foster the cloth industry, or the modern regulative system of protective tariffs. This complex of factors may give an industry a momentum which carries it forward after the original forces have grown weaker or even disappeared, with the result that after a district has had a long start it may go on growing at the expense of other districts which, under the conditions of later years, might have proved at least as attractive if a new start had been possible.

### TEST PAPER VIII

1. Explain the function of manufacture.
2. What, in your opinion, are the leading characteristics of modern manufacture?
3. Explain how manufacturing occupations differ from constructive occupations, and give three examples of each type.
4. What are the relations existing between the extractive and the manufacturing industries?
5. State the chief requisites of successful manufacture.
6. Contrast the manufacturing with the extractive industries.
7. What have been the effects of Capital and Division of Labour upon the development of modern manufactures?



## CHAPTER IX

### ORGANISATION OF A MANUFACTURING BUSINESS

THE organisation of the business of a manufacturer is more complex than that of a commercial house, since its functions are more numerous. Many differences also occur which are consequent upon the nature of the undertaking: that is, whether it is engaged in extraction, construction, or purely in manufacture. The conduct of a manufacturing business requires, in addition to commercial experience, a technical knowledge of the business, and in such an undertaking there should be a distinct commercial and a distinct technical management.

**ORGANISATION OF A MANUFACTURING CONCERN.**—The organisation may be separated into the following departments—

#### **I. Business Management and Stocktaking—**

(a) The procuring, improving, and the maintenance of the business equipment.

(b) The supervision and checking of the stock and stocktaking.

(c) The engagement and dismissal of workmen.

(d) Arrangements for the welfare of the staff.

(e) Administration of the workmen's insurance under the National Insurance schemes.

(f) The classification of time and piece rates.

#### **II. The Administration of the Raw Materials—**

(a) The determination of the requirements of raw materials.

(b) Asking for quotations and the placing of orders.

(c) The receiving and checking of the incoming materials and goods.

(d) The checking and entering of the incoming invoices.

(e) The keeping of the stores.

(f) The giving out of raw materials and their corresponding entry.

#### **III. Manufacturing or Technical Administration—**

(a) The making of drawings and plans of construction.

(b) The preparation of the lists of raw material and wages for the calculation of costs.

(c) The fixing of the dates for the completion of the work.



- (d) The supervision and allocation of the work.
- (e) The examination and passing of the finished work.
- (f) The delivery of the finished goods to the warehouseman.

#### **IV. Wages and Costs—**

(a) The checking of the wages sheet and the keeping of the Wages Book.

- (b) The making out of wages list.
- (c) The preparation of the lists of material used and of wages.
- (d) The determination of primary costs.
- (e) The determination of final costs.

#### **V. Quotation and Sale—**

- (a) Propaganda and advertising.
- (b) Arrangements with travellers and representatives.
- (c) The giving of quotations.
- (d) The making of inquiries respecting prospective customers.
- (e) The acceptance and confirmation of orders.
- (f) The keeping of a register of customers.

#### **VI. The Organisation of Accounts—**

- (a) The management of cash and bill transactions.
- (b) The keeping of the principal books including the general and private ledgers.
- (c) The giving out of the contract numbers.
- (d) The keeping of the Contract Books.
- (e) The keeping of the Works Accounts.
- (f) The preparation of the Profit and Loss Account and Balance Sheet.
- (g) The preparation of the outgoing invoices.

#### **VII. Warehouse Administration and Dispatch—**

- (a) The receiving and storing of the manufactured goods.
- (b) The preparation of the goods for dispatch.
- (c) The procuring of packing materials and the packing of the goods.
- (d) The arrangement and supervision of the transportation.
- (e) The preparation of the shipping documents.
- (f) The forwarding of the goods.

In the diagram on page 85, the Managing Director controls the undertaking through a Financial, Technical, and a Sales Executive, so that the technical or manufacturing side of the business is kept quite separate from the commercial. In small



or moderate-sized businesses, the management of both the commercial and technical sides of the business is often vested in the hands of the same person, although such a union ought, if possible, to be avoided in the interests of successful organisation, for the interests of the commercial side are totally different from those of the technical.

In his work of management, the head of a manufacturing concern has to keep in mind the technical side of the business, and from the commercial side he acts as a receiver for the whole of the raw materials consumed in the works, and for the wages and expenses of management; he also acts as a supplier of the goods, which have resulted from the expenditure on wages, materials, etc.

**Need for the Correlation of Functions.** The technical side of the business requires from the Financial Executive materials at low prices and of good quality, the careful examination and regulation of wages and expenses; and from the Sales Executive the disposal of the goods at profitable prices. On the other hand, the Financial Executive requires from the Technical side an account of and proof of the existence of stock, and of the manner in which wages and materials have been used, together with a rational and economical system of production. It is the duty of the manager in charge of the Buying Department to see that the raw materials are purchased as cheaply as possible, and that they are carefully administered so that the sale of the manufactured goods may be effected to advantage. This can be ensured, however, only when the works manager exercises a careful administration of the raw materials by the execution of good workmanship, which results in a reasonable cost of production.

The *Works Manager*, in supervising the manufacturing processes, must see that there is a well-equipped workshop, which must be kept in order and up to date. His main object is to turn out the goods in the best possible condition and at a price which can withstand competition. For this purpose, it is necessary that he should have a good knowledge of the technical side of the business, as well as organising ability.

**Treatment of Workmen.** If a manufacturing business is to meet with permanent success, the works manager must be straightforward and honest in his dealings with his workmen, and must



take an interest in their general welfare. Workmen who have confidence and respect for their employers usually believe they will receive a fair reward for their labour, and may remain satisfied when a temporary reduction of wages is necessary on account of an unfavourable state of trade.

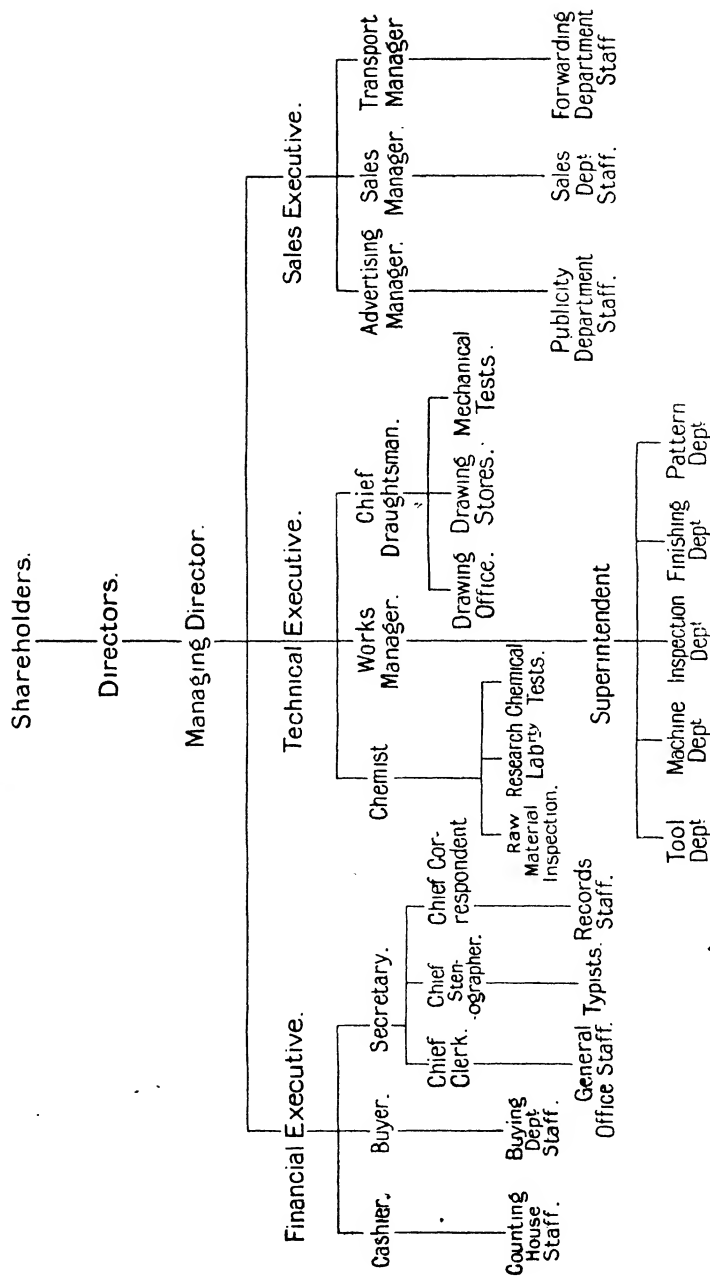
From the point of view of business organisation, it is imperative that there should prevail at the head, specialised knowledge, ability, and justice. For the exercise of the last-named the first two are essential. Even where such qualifications do exist, however, misunderstandings and grievances often arise; and where favouritism is spread abroad, intrigues and envy are of daily occurrence. With such drawbacks, any business organisation must naturally suffer, and laziness and falsehood will tend to triumph over industry and uprightness. To avoid this state of things, a proper system of division of labour must be introduced, according to which each employee has allotted to him a definite sphere of work for which he is responsible and on which he has to concentrate his whole attention.

**Example of the Delegation of Responsibility.** The diagram on page 85 will illustrate the method according to which responsibility may be delegated in the case of an extensive manufacturing business, although the same plan may be followed in the organisation of smaller undertakings. At the head of the concern is the Managing Director, to whom are directly responsible the Financial, Technical, and Sales Executives. To each of these sectional heads are linked the managers of the departments, by whom duties are further delegated to their subordinates. Whilst each department of the business operates quite independently of the rest, it is at the same time linked up systematically to the Managing Director through the personal control of each sectional Executive.

**FLEXIBILITY OF MANUFACTURING SYSTEM.**—Practically every manufacturing concern buys, to some extent, not merely raw materials, but also finished parts and complete articles, and only rarely does an undertaking manufacture everything it sells right up from the raw material stage. The question sometimes arises as to the desirability of buying what one has hitherto been in the habit of making, or how far it is desirable to begin making what one has been in the habit of purchasing.



# ORGANISATION OF A MANUFACTURING CONCERN





A manufacturer is primarily guided in such matters by what pays best, although this is only one side of the matter. If the Managing Director is to look ahead and consider the business for the future, he must remember that the object is not merely to keep in touch with the immediate requirements of customers, but also with their changing desires and needs.

In deciding whether to modify the nature of his output, the manufacturer's first inquiry will be to ensure that he can conduct the business at a profit under the changed circumstances, for, unless that is the case, the undertaking cannot last indefinitely. On the other hand, he should not be too imperative about temporary losses, for, as a rule, no great success can be made without incurring some initial losses. Expenses such as advertising, establishment expenses, etc., may at first appear to be losses, since they are expenditure incurred in the deliberate object, not of earning profit at the moment, but for the future.

The manufacturer's position is rendered all the more difficult if the kind of goods he is in the habit of dealing in is one for which there is a fluctuating demand, or is manufactured out of raw materials of which there is a fluctuating supply. This seems to suggest that the Technical or Manufacturing Department must take its place in any organised scheme midway between the Buying Department and Sales Department. (See diagram, page 85.)

The *Sales Department* should always be endeavouring, not merely to get orders for standard lines of goods, but also to ascertain in advance the varying demand of customers, so as to be supplied beforehand with the new kinds of goods that they are likely to require. This is a commonplace when dealing with fashions and seasonable goods, but it applies also to standard goods, since they are liable to change slowly. A Technical or Manufacturing Department is entitled to look to the Sales Department for information upon these points, and it is not the exclusive duty of the Manufacturing Department to consider the precise kind of goods that it has to make. Again, if the Manufacturing Department is not prepared to make goods at a price stipulated by the Sales Department, then the latter may deal directly with the Buying Department, which will purchase many other articles for sale, as well as the raw materials of manufacture.

The *Manufacturing Department* should keep in touch with the



*Buying Department* not merely for the sake of ensuring that it can always get a supply of the materials required in connection with its output, but also because, if it is going to be up to date and progressive in its ideas, it will be continually considering the practicability of applying new methods to manufacture. This often involves the use of different materials in place of materials which have become difficult to obtain or can be obtained only at considerably enhanced prices.

**DISTRIBUTION OF MANUFACTURED GOODS.**—The distribution of the goods of a manufacturing business will now be considered in so far as it relates to the home trade, whilst that of the export of manufactures will be dealt with later. Of recent years, many manufacturers have eliminated the services of the various intermediaries and sell their product directly to the actual consumers.

There are various channels which may be chosen by the manufacturer in the distribution of his output, the chief of which are shown on the diagram on page 88. He may sell—

(a) Directly to the wholesaler, who organises the market and distributes the goods to the retailer.

(b) Directly to the retailer. There is a growing tendency for manufacturers of boots, shoes, hats, etc., to distribute them through their own retail stores.

(c) Directly to the consumer. This method has largely resulted from development in advertising, which has given rise to the rapidly developing mail-order business.

(d) Directly to a Commission Agent, who either distributes through the retailer or sells directly to the consumer. Many goods such as pianos, typewriters, sewing machines, agricultural implements, and motor-cars are especially adapted to this method.

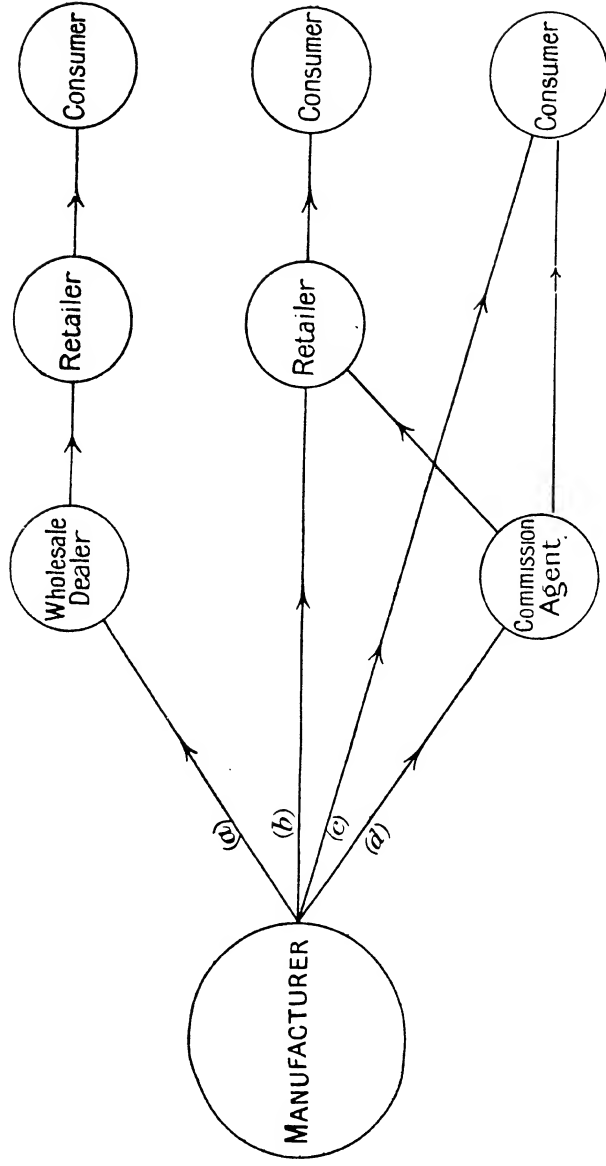
(e) Direct through a selling association. Since the war many manufacturing undertakings have combined into co-operative selling associations, usually under the leadership of a large firm. The object of this method of organisation is to procure a uniform expert policy amongst the various manufacturers who enter the association. Such selling associations often devote themselves at first to the home market, but, subsequently, they extend their operations to foreign countries, where they are able to establish a firm footing by the founding of their own branches.



MANUFACTURER'S CHANNELS OF DISTRIBUTION IN THE HOME TRADE

I. MANUFACTURER.

II. Wholesaler. III. Retailer. IV. Consumer.





The choice of methods will depend largely upon the kind of commodity produced and the nature of the demand for it. For instance, if it is an article which can be sent easily through the post, the wholesaler and retailer may be eliminated through the establishment of a mail-order business. It is very seldom the case, however, that a manufacturer adopts any one of these methods to the exclusion of all the others, but all the methods are usually in operation concurrently.

### TEST PAPER IX

1. Why is the organisation of a manufacturer's business more complex than that of a commercial house?

2. Into what departments may the organisation of a manufacturing concern be divided?

3. Explain the need for a proper system of correlation between the various departments of a manufacturing concern.

4. Describe the method by which responsibility is delegated in a large manufacturing business.

5. Discuss the chief methods adopted by the manufacturer in the distribution of his finished products.

6. Elucidate, with illustrations, the reasons why particular industries become and remain localised in particular districts or countries.

7. Trace the effect of the adoption of mechanical methods and of the growth of large-scale operations in any one branch of industry.

8. Draw out the distinction in meaning between "industry" and "manufactures."

9. Sketch the organisation of a staple industry, such as the cotton industry, indicating the links in the chain of production and distribution from the growing of the raw materials to the selling of the finished goods in the shop.

10. Using for the purpose of illustration some manufacturing industry with which you are familiar, explain the business machinery that has been developed for the purchase of its raw materials and for the sale of the goods it manufactures.

11. What is meant by business organisation? You are called upon to organise a manufacturing business. Assuming that you have control of twenty persons, state how you would delegate their duties with the object of ensuring the maximum output and efficiency.

12. Describe carefully the organisation of any manufacturing business with which you are acquainted under the following headings—

(a) The division into departments.

(b) The delegation of duties among the members of the staff.

(c) The function of the business in relation to the outside world.

13. "Efficient organisation is the basis of successful enterprise." Discuss this statement and show how you would organise the commercial side of a large manufacturing business, indicating the chief functions of the various departments.



## CHAPTER X

### COMMERCE AS A BRANCH OF PRODUCTION

UP to this point the extractive industries and those of manufacturing and construction have been dealt with, and now the functions of the third branch of industry, viz., commerce, will be analysed. A treatise on the theory and practice of commerce must deal, not with the manner in which commerce might be conducted in an ideal state, but how it actually is conducted in the world around us, so that it will be necessary to trace its historical evolution and to examine how it is actually conducted under existing circumstances.

**PRIMITIVE COMMERCE.**—It must be remembered that in an organism each of its parts must work for the furtherance of the whole well-being, and in this way each member will receive rights corresponding to the duties which he performs. This general organic law is certainly applicable to business in general, and especially in relation to commerce. Commerce must justify its existence by the services which it renders to the whole economic organism. The extent to which it has done this is to be seen from its historical development. For this purpose a glance will be taken at the oldest form of commerce—the direct exchange of products between individuals, which must have existed among the cave dwellers of the Stone Age. This can be inferred from the fact that caves have been discovered in which flint tools have been manufactured ; and as such tools have been found in all cave discoveries, there is evidence of the existence of a system of exchange based on the separation of employments. The origin of this system of exchange is not difficult to trace. Some cave dwellers, who happened to live in the vicinity of quarries containing flint, and learned the manufacture of flint tools, naturally produced a stock of such goods. A neighbouring cave dweller when out on his hunting expeditions would learn of the importance of these new tools, and the desire would naturally be created within him to possess some of them, and since he was in possession of a stock of bear skins for which he had no use, it is clear that he would persuade the possessor of the tools to make an exchange. The latter would be glad to possess a bear skin to protect



himself against the weather, and would be willing to give in return a flint knife. Thus the first transaction is concluded.

The greater the distance of the hunting fields from the stone quarries, the less possible it is that these two parties will produce for themselves the articles of exchange. The knowledge of the new tools with which it is possible to kill wild beasts, fell trees, make boats and a hundred other things, is soon carried from neighbour to neighbour and from cave to cave. As everyone is desirous of procuring a stone axe there arise intermediaries who facilitate the exchange of the products. A point to notice is that each party to this primitive exchange has improved the conditions of his labour and of his mode of existence. The cave dweller in the hunting district is now able to kill with greater success the wild beasts which surround him, and thus render his life more comfortable ; the other party is able to make use of the bear skins as a protection against the cold winds, so that his efficiency is increased and his comfort augmented. Each gave to the other of his superfluities and both were rendered more efficient in production and should thereby satisfy their wants to a greater extent.

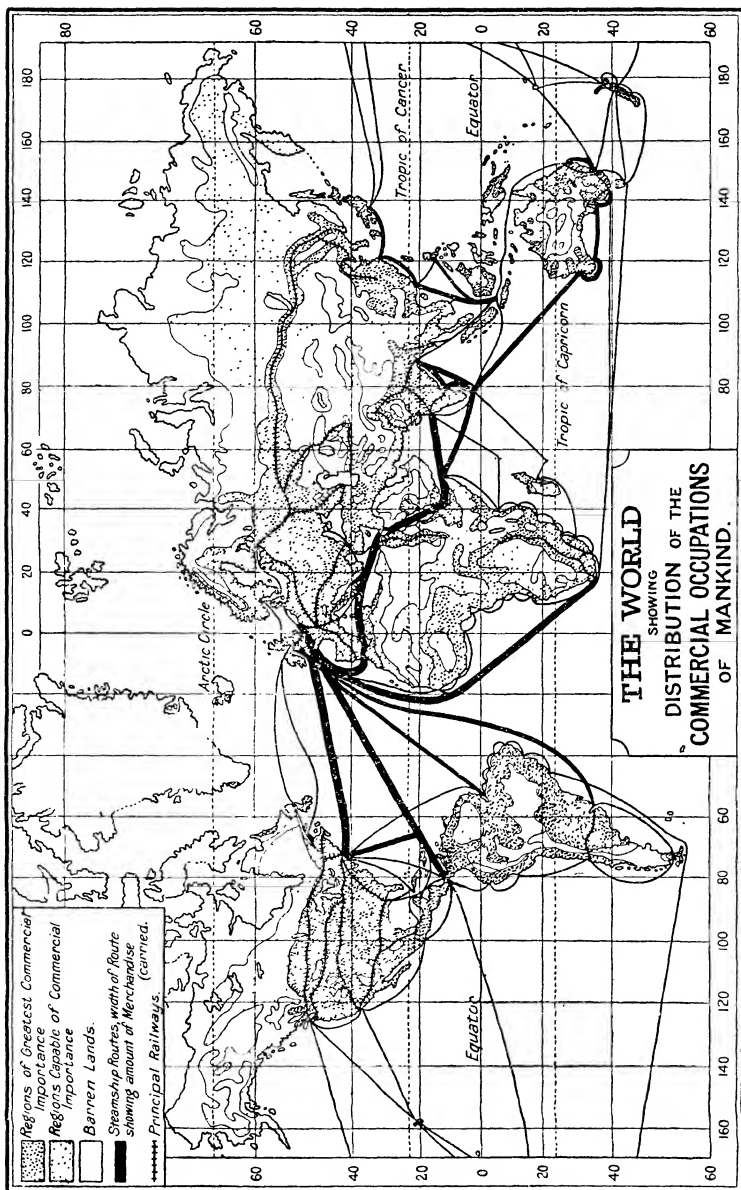
#### **SIMILARITY BETWEEN PRIMITIVE AND PRESENT-DAY COMMERCE.**

—At the present day, with the economic development of the world, the basic principles of commerce are practically the same as those which existed among primitive men. The watchmaker of Switzerland and the farmer in Australia, stand in a similar relationship to each other as did the early Paleolithic men. The sheep farmer sends to the watchmaker the wool out of which the latter may obtain his clothes and thus protect himself from the rough mountain climate. In return for this, the watchmaker gives an artistically manufactured watch with which the shepherd can, among other things, measure the time with a greater degree of exactness than if he were unable to obtain possession of a watch. Both benefit from the exchange, their efficiency is increased, and their method of living is improved.

The main distinction between the transactions of primitive times and those of to-day is the introduction of two new factors which facilitate exchange, viz. *money*, and a specialised person known as a *trader*.

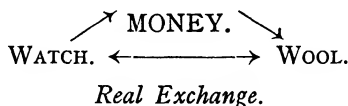
Money does not alter the nature of exchange. It can conceal only the nature of the original transaction, for the exchange now becomes







a double operation—a sale for a price expressed in terms of money and a purchase for money. The money with which the Swiss watchmaker paid for his wool was the money he received for the watches sold by him. In the same way the Australian sheep farmer obtained his purchase money for the watch in return for the wool produced by him. Hence in modern commerce every exchange is effected indirectly through the medium of a third commodity, i.e. money



The real exchange is that of a watch for a quantity of wool, although this is effected in the twofold operation—

- (1) Sale of the watch for money.
- (2) Purchase of wool for money.

The intervention of money in the exchange of goods conceals and renders more complex what was originally a simple transaction, but nevertheless it still remains an exchange of commodities between the parties engaged in production. *Money represents nothing more than a receipt for services rendered to society with which a corresponding quantity of the services of others can be obtained.* The exchange of labour is on the whole equivalent to an exchange of products, so that money does not dispense with the principles involved in the exchange between primitive men. The intervention of an intermediary or trader, in the operations involved in exchange, does not alter the original basis of exchange. The intervention of the trader is founded on the expansion of the local business to the town, country, and finally to the whole world. The Swiss watchmaker does not know the Australian farmer, nor does he even consider that he is engaged in helping to supply his needs. In the same way the sheep farmer is unaware of his dependence upon the watchmaker. Both work for each other, enjoy each other's products, without recognising their dependence upon each other; in consequence, a third person must bring about the organic union of the two parties. The trader appears in both cases as a purchaser of the goods produced in excess of local needs, and pays for them in terms of money. On the other hand, he also acts as seller and receives money in return for his goods. Taking the original



form of trade as a basis, we see that both parties are brought together by the intervention of a third person, and it is clear that the trader pays the one producer with the money which he has received from the other. The exchange of products is in practice brought about in this way.

COMMERCE WIDER THAN TRADE.—The meaning of "commerce" is much wider than that of "trade," and embraces all those processes which help to break down the barriers between producer and consumer. It has just been shown that the "trader" effects the exchange of the goods by carrying out the purchase and payment for the same. There are, however, two other operations involved in nearly every commercial transaction—

(1) *The alteration of the position of the goods, which necessitates transport and insurance.*

(2) *The accumulation of commodities, which necessitates "warehousing."*

The distribution of goods between the producer and the consumer has therefore to encounter the threefold hindrances of "persons," "place," and "time."

The *personal hindrance* is surmounted by the function of exchange. Since there is a common medium of exchange and measure of value in the form of money, it follows that the exchange resolves itself into one of purchase. The purchase consists of two transactions—the offer of the goods, and their acceptance at an agreed price, i.e. the payment. On account of the separation of these two transactions, with regard to time and place, not only is credit involved but also the means of making remittances, such as the payment of cash, postal and money orders, cheques, etc. From this it follows that within the scope of commerce is embraced the money market, and more especially the whole of our banking system.

To overcome the *separation of place*, another special organisation is necessary, viz. *a system of transport and insurance*. The means of transport will naturally vary according to circumstances, and may be by road, river, canal, rail or by sea. During the period of transportation, the goods will be subject to many risks of fire accident, and perils on land and sea. Hence the various kinds of transport and insurance will be involved.

A further economic activity is necessary to surmount the *separation of time* existing between production and consumption which



arises on account of the intervals between the harvests and the separation of the places of production and consumption. This necessitates the accumulation of stocks for future requirements, which gives rise to the various branches of work embraced under the heading of "*warehousing*."

From what has been said may be formulated a definition of commerce which has reference more especially to its functions than to its scope. **Commerce is the sum total of those processes which are engaged in the removal of the hindrances of persons (trade), place (transport and insurance), and time (warehousing), in the exchange (banking) of commodities.**

In the removal of these hindrances in the way of exchange there are, therefore, four separate functions concerned in its organisation, viz. trade, banking, transport and insurance, and warehousing. Commerce is, therefore, seen to be an organised system for the exchange of goods between the members of the industrial world, and may be regarded as the last link in the chain of productive activity.

### TEST PAPER X

1. What evidence is there that trade existed among the cave-dwellers of the Stone Age ?
2. Compare and contrast primitive and modern commerce.
3. In what respect does the meaning of "Commerce" differ from that of trade ?
4. "Commerce is the sum total of those processes which are engaged in the removal of the hindrances of persons, place, and time in the exchange of commodities." Explain carefully the meaning of this definition of commerce.
5. Analyse the various operations involved in every commercial transaction.
6. What auxiliary services does "trade" call into existence ?
7. Show the relationship between "Industry" "Commerce" and "Trade."
8. Divide commerce into its various branches, and explain the function of each.
9. What in your view is the purpose of commerce ? Show how the different occupations, properly termed commercial, help in the attainment of this purpose.
10. Compare the present social state of England with that of Englishmen in the past or of savages to-day, and show, with reference to that comparison, the nature of modern commerce.
11. State precisely the difference between Commerce and Industry. Set down the branches of Commerce in two groups, of which one shall contain what you consider to be the principal services and the other the less important of the services rendered.
12. It is said that there is a wide gap between the producer and the consumer. What methods are adopted with the object of bridging this gap ?



## CHAPTER XI

### INDUSTRY IN GREAT BRITAIN

FOR more than one hundred years Great Britain has been the most important manufacturing and commercial country in the world, although its predominance in this respect is now being seriously contested by other Powers, particularly the United States. This industrial prosperity is due in no small measure to natural advantages. On account of its situation as the centre of the land hemisphere, and midway between the civilised States of Europe and America, Great Britain may be said to hold the most favourable position in relation to the world's commerce. The country is highly favoured by its sea-board, estuaries, and harbours, its soil and climate, with their respective variations, and its mineral resources. The coast-line is much indented with numerous bays and river mouths, stretching far into the interior, combined with a remarkable river and canal system which facilitates industry in a high degree. Harbours are scattered along the coast and near to the estuaries, and render great assistance to ship-building and the conduct of sea-borne trade, whilst the shallowness of the surrounding seas has given rise to valuable fisheries. The physical features consist partly of flat, fertile land, as in the South-east of England, and partly of highland, as in the West and North-west of England and in Scotland, where the chief mineral deposits are to be found. Further, the constituents of the soil and the moist, equable climate are by no means the least important factors in determining the industrial prosperity of the country, for they are favourable to the fertility in plant life and to the vigorous growth of animal life. In addition to these great natural advantages, the power and civilisation of Great Britain are also dependent upon the peculiar physical and mental characteristics of its people, which are marked by their practicality, their desire for enterprise, their coolness and perseverance.

The concentration of the population of England is higher than that of any other European country, except Belgium and Holland, it being found chiefly in towns; whilst in Scotland and Ireland there is only a medium density.



**CLASSIFICATION OF BRITISH OCCUPATIONS.**—In accordance with the basis of classification, as explained in an earlier chapter, the occupation of the people of Great Britain may be divided into the following classes of industry—

- (1) Extractive.
- (2) Manufacturing and Constructive.
- (3) Commercial.
- (4) Direct Services.

In consequence of the great urbanisation of the population, the extractive are less important than the manufacturing industries. About 33 per cent of the persons employed in the country are engaged in extractive occupations ; 46 per cent in manufacturing and constructive ; and about 21 per cent in commerce, which is the highest percentage of any country.

**Extractive.** For the purposes of *agriculture*, the land of Great Britain is divided into a number of large estates, which are usually split up into farms and leased out by their owners to tenants, who pay a stipulated rent in return for their holding. This is known as *tenant-farming*, and differs from that of some Continental countries in that there is a complete absence of independent peasants owning their own holdings. The method of cultivation which mostly prevails is that of the intensive system, although the actual area under tillage represents but a small portion, the land being used for more profitable purposes.

*Tillage* and *market gardening* are estimated to cover about 24 per cent of the whole area of the country, whilst *tillage alone* represents about 13 per cent. This state of affairs is the fault neither of the soil nor of the climate, nor of the people, but is chiefly due to the vast increase of imported food-stuffs which can be produced elsewhere in greater abundance and sometimes at less cost, and which are admitted into our seaports free of duty. The climate is moist, with moderate heat and cold, and is much more favourable to the rearing of live stock than to the growth of cereals. The grass is so rich that no other country can produce finer cattle, finer sheep, or finer horses.

*Afforestation* is almost insignificant, only about 4 per cent of the area being covered with forests (which are located chiefly in Scotland), whilst *pastures* and *meadows* cover about 54 per cent of the entire country. Of great importance, also, is the yield of fish—







notably that of herring off the East Coast, near Yarmouth; and near Wick, in the northern part of Scotland; cod is caught off the Dogger Bank; the oyster fishery is restricted chiefly to the mouth of the Thames; whilst the whale fishery is conducted from Dundee.

The existence of large quantities of *minerals* has led to the establishment of extensive *mining* operations. Copper, tin, lead, manganese, china clay, and other minerals are found in various parts; and gold is found in Wales. But the deposits of coal and iron in which Britain abounds have in more recent times been the main-spring of industrial prosperity. The application of these two minerals to the manufacture of all kinds of machinery, of which British people were the inventors, gave to this country the start of other nations, and placed her in the vanguard of industrial activity. The iron and coal in Great Britain are generally found in proximity to each other—a fact which adds greatly to the facility of working the mines and of turning their resources to practical account.

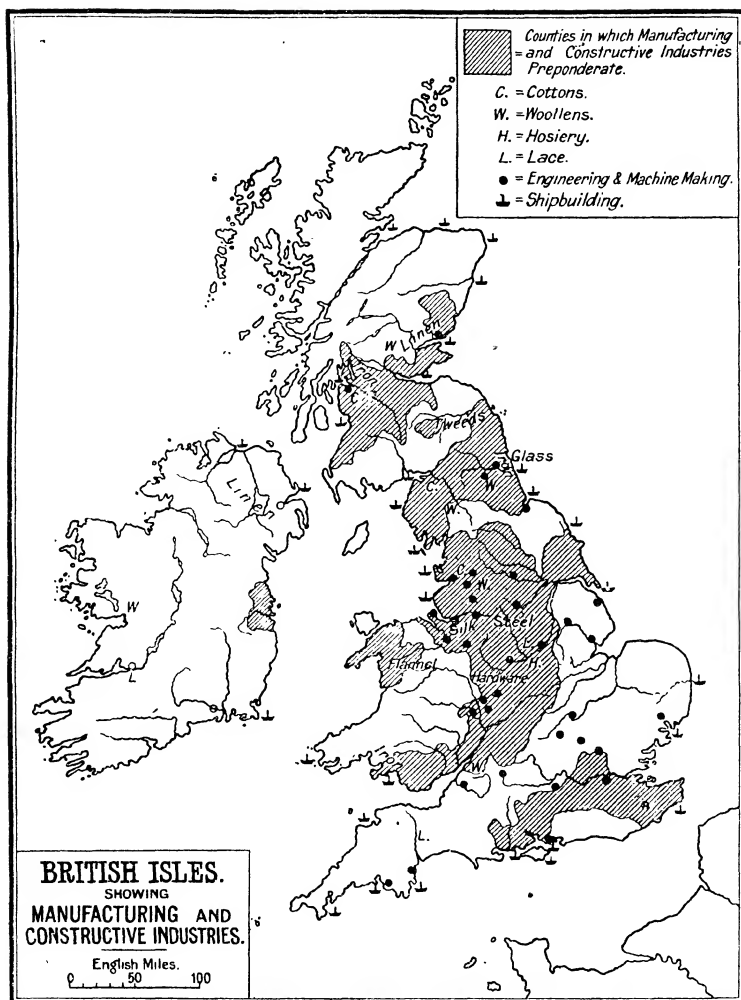
The chief areas of coal-mining are situated in the neighbourhood of Whitehaven, Newcastle, Shields, Sunderland, Manchester, Sheffield, Birmingham, South Wales, and Bristol; the principal iron-producing areas are the same districts, or in close proximity thereto, as well as the Furness district of Lancashire and the Cleveland district of Yorkshire.

The output of both coal and iron in Great Britain long exceeded that of other countries, but of late years it has been surpassed by the United States, and, with regard to iron, by Germany in more recent years.

**Manufacturing and Constructive.** The manufactures of Great Britain are the oldest of the modern large-scale industries, and, owing to the abundance of suitable raw materials, the early introduction of industrial freedom, the inherent capacities of the people, the favourable position of the country with regard to exchange, and a series of other fortunate circumstances, the country was soon enabled to establish itself as the leading manufacturing nation of the world.

The most important manufacturing region is that of a line passing through the towns of Manchester, Birmingham, Leeds, and Sheffield. The chief branch of manufacture is that of textiles, which, in magnitude, variety, and efficiency is without equal, and,







in consequence of the moist climate, is (in many branches) likely to remain unexcelled. The centres of the cotton manufacture are Manchester, Blackburn, Preston, Glasgow, Belfast, etc.; the woollen industry is centred in Leeds, Bradford, Halifax, Huddersfield, Glasgow, etc.; the linen industry is specially located in Ireland (with its centre in Belfast), in Dundee, Forfar, Barnsley, Leeds, Liverpool, etc.; the silk industry in Cheshire, Lancashire, Yorkshire, London, etc.; lace-making and hosiery-making in Nottingham, Leicester, etc.; carpet-making in Kidderminster, Wilton, etc. Almost rivalling the textile industry in importance is the manufacture of *iron*, *steel*, and *metal goods*, the construction of *tools* and *machinery*, which is carried on mainly in the vicinity of the coal-fields, or near to the iron-smelting centres. The principal areas of production are in the neighbourhood of Birmingham, Sheffield, Wolverhampton, Newcastle, London, Glasgow, etc. Other manufacturing and constructive occupations of great importance are ship-building, with its allied branches, at Newcastle, Shields, Glasgow, Greenock, London, Liverpool, Hull, etc.; pottery in the Pottery District, with its centre at Stoke-upon-Trent; paper and leather, chemicals, clothing (with its centre in London), brewing, confectionery, and employment connected with the preparation of food and luxuries.

**Commercial.** In spite of increasing competition and widespread restrictions imposed by governments, the commercial activities of Great Britain are of the greatest importance. A considerable volume of commodity imports is obtained from all parts of the world, notably in the form of raw material and foodstuffs. In exchange, exports take the form of one important raw material—coal—and a wide range of manufactured products. In respect of this commodity trade, however, Great Britain has long had an “adverse” balance, where imports exceed exports. During the years of depression following 1931 this was reduced, partly through the contraction of international trade, and partly as a consequence of the tariff policy under the Import Duties Act, 1932. Since 1936, the adverse balance has once more increased mainly as a consequence of rearmament.

Commodity trade is, however, only one form of commercial activity and the country enjoys an important source of income from the performance of services. Prior to the depression of 1931, this was sufficient to pay for the surplus imports and leave a balance in



our favour. Of recent years it would appear that we have not been so fortunate and income from this source has been inadequate to make good the difference. The principal items of revenue from services—the so-called “invisible items”—are as follows—

1. *The Amount Due for Freight.* Even though the British mercantile marine has fallen in relative importance as compared with the merchant shipping of other countries, a substantial net revenue is derived from freight payments. This fell heavily during the depression, but recent years have seen a recovery and in 1938 it was estimated that £100 million were received from this source.

2. *Income from Overseas Investments.* Long years of profitable trading abroad gave the people of Great Britain substantial sums to invest in overseas countries. These investments took the form of loans to foreign governments and municipalities as well as investments in the shares and debentures of all kinds of trading concerns. Year by year, interest and dividend payments yield a substantial income which was valued in 1938 at £200 million—an amount, however, which falls short of the value in pre-depression days.

3. *Receipts from Banking and Insurance.* Under this heading may be included commissions paid to dealers in the numerous commodity markets of London who complete contracts of purchase or sale on behalf of overseas customers. In a large number of cases such dealings are also financed through the medium of the British banking system which earns profits and commissions for the services which it renders. Further, these services are often employed in respect of transactions entirely between overseas countries. Finally, British insurance companies transact a large volume of business on behalf of foreign clients, and this involves the receipt of premiums. In all, these various sources of income produced £35 million in 1938.

In addition to the above-mentioned classes of income from services, there are certain miscellaneous sources of income such as that from tourist expenditure, and film royalties, which augment the total. In 1938 these miscellaneous items were estimated to produce £10 million though the figure is generally admitted to be a very rough approximation.

**Direct Services.** It has already been seen that many human desires can be satisfied only by direct personal service. For example, the desire for enlightenment calls for the services of the teacher, preacher, or writer ; the cravings for amusement are







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This map is only intended to give a general idea of the exports of the countries named, and the British ports to which they are sent.







satisfied by the music-hall artiste or the cinema operator; the desire to be freed from pain gives rise to the personal services of the doctor, dentist, or nurse; whilst the fear of invasion and need for protection generally call for the services of soldier, sailor, judge, etc. According to the Census returns, there was at one time an enormous increase in the proportion of those engaged in the performance of direct services, and this was particularly evident in the numbers of those engaged in teaching and those engaged in domestic service. From this, it would seem that the country was growing wealthier, and a greater and greater share of the national dividend could be spared from the actual production of food, clothing, and shelter, in order to develop the more aesthetic side of man's nature. With the application of steam to machinery and the introduction of numerous mechanical inventions, labour had been rendered more efficient and the work of the country more highly organised—hence the increased expenditure upon personal or direct services. The war, unfortunately, put an end to this development, and there is no doubt that the country is now much poorer than it was a few years ago.

**RECENT TRENDS IN BRITISH INDUSTRY.**—Although the advantages enumerated above have served to give Great Britain a substantial lead over her industrial and commercial rivals, even before 1914 her supremacy had received a strong challenge. As a result of a number of factors of great complexity arising partly out of abnormal war-time conditions, her difficulties have been intensified in recent years. Dependent as she is upon overseas markets for the prosperity of her great staple industries, it is inevitable that the disturbed international conditions since 1918 should have proved injurious to her trade. Political disturbances, currency fluctuations, and protectionist policies have been widespread, and are, one and all, detrimental to the smooth flow of international commerce. In addition to these external difficulties, however, British industry has had to contend with troublesome problems of internal readjustment, many of which still await final solution.

Yet, in viewing the position and progress of British industry at the present day, it is easy to be misled into false conclusions of an over-pessimistic nature. The commanding industrial lead gained in the last century over other countries has not been maintained, but a moment's consideration is sufficient to show that it was not



possible to maintain it when other nations began to devote their energies to industry and commerce as assiduously as Great Britain alone had previously done. The acid test of economic success is to be found in the standard of living of the inhabitants of the country, and it is manifest to all that the average standard of comfort in this country has risen immensely as the result of its industrial prosperity in the last half century. It is no slight thing that these islands, unable even to provide their present inhabitants with the means of life, to say nothing of luxuries, have created exchangeable wealth with which not only the means of sustaining existence but also an ever-rising standard of refinement and comfort have been obtained.

The growing competition of foreign industries assisted by Government intervention in the form of tariffs and subsidies has created prolonged depression and unemployment in the exporting trades such as coal, metals, engineering, and textiles. This depression has to a considerable extent distracted attention from developments in other fields and has engendered an over-pessimistic attitude. Amongst some of our old established industries such as agriculture, fishing, and domestic service, the figures of the 1931 Census show an inability to expand employment further, whilst in some cases a contraction has occurred. In the case of the leading industries of the industrial revolution, again, which were the great labour-absorbing industries of the nineteenth century, we find no additional employment, and often contraction. Contracting employment in some cases, however, merely marks a correction of abnormal developments during the War, when iron and steel, engineering and ship-building were expanded beyond peace-time needs.

If now we turn to the group of technical manufacturing industries, mainly dependent upon recent invention, such as rayon, radio, motor, cycle, aircraft, chemicals, and so on, we find very substantial development of capacity to absorb labour. The records compiled by the Ministry of Labour in connection with the unemployment insurance scheme show that in a matter of nine years the numbers employed in electric wiring and contracting expanded by 110 per cent, silk and artificial silk by 67 per cent, and public works contracting by 88 per cent. But factory industry, which is usually highly mechanized, tends to supply a dwindling proportion of new employment. The larger and increasing share is provided by the



group of industries and services dealing with assembly, organization, processing, and distribution. Water supply, gas and electricity supply, road passenger transport, telephones, broadcasting, laundries, hotels, and cinemas are all occupations of a new and expanding type. The physical handling of goods between the factory and the ultimate consumer again gives employment to a rapidly expanding labour force in shops, warehouses, and road delivery services.

### TEST PAPER XI

1. To what extent is the industrial prosperity of Great Britain due to natural advantages?

2. Into what four classes may the occupations of the British people be divided?

3. Enumerate the leading extractive occupations of Great Britain.

4. What are the chief factors which determine the distribution of the British manufacturing and constructive industries?

5. Explain what is meant by invisible exports, taking, as an example, the transactions between Great Britain and the United States.

6. "Imports must be paid for by exports." Explain this statement, and consider what must be included under each heading to make it true.

7. What conclusion would you draw from the great increase of recent years in the proportion of persons engaged in the performance of direct services in the British Isles?

8. According to the Census of Occupations, 1931, the total population of England and Wales (in millions) was 39.9. Persons over 14 years of age employed in Extractive Industries amounted to 2.1; in Manufactures, 4.6; in Commerce, 5.5; in Direct Services, 3.7; in Undefined Occupations, 1.6; and Retired and Not Gainfully Occupied, 10.8.

Illustrate these figures by means of a diagram, and express the various classes of occupations as a percentage of the total occupied population.

9. Show, from your knowledge of the industries of Great Britain, that Commerce is always closely connected with extraction or manufacture.

10. Enumerate twenty different callings in the neighbourhood in which you live, and classify them.

11. Account for the localisation of industries in Great Britain by reference to particular instances.

12. "All the men of all lands have become necessary to one another for the exchange of the fruits of industry and the products of the soil." Discuss the above statement with special reference to the British Isles.

13. Is it true that England is being impoverished by her foreign trade, because the imports largely exceed the exports in value? Account for the excess in value of the imports.

14. What, in your opinion, is the recent trend in British industry?

15. "The restriction of imports by the United Kingdom and the embargo on foreign loans in 1931 has resulted in cheap money and stimulated home trades; but certain important industries experience dwindling foreign markets each successive year." Explain and elucidate this statement.

16. How do economists understand the terms Production and Distribution? Does the so-called "distributive" trade, such as shopkeeping, pertain to production or to distribution in the economist's sense of these terms? Give reasons.



## SECTION III—COMMERCE

### CHAPTER XII

#### THE EARLY HISTORY OF COMMERCE

THE historical development of commerce may be divided into two great periods: Early Commerce and Modern Commerce.

Early Commerce may, for convenience of treatment, be further grouped into three subdivisions—

I. The Period of Antiquity, lasting from prehistoric times to A.D. 476.

II. The Middle Ages, lasting from A.D. 476 to A.D. 1453.

III. The Period of Discovery, lasting from A.D. 1453 to 1760.

**COMMERCE IN ANCIENT TIMES.**—The beginning of trade stretches back into prehistoric times. In the simplest state of civilisation, when each family merely looked after its own needs, trade and commerce were neither necessary nor possible. The progress of nations and of tribes from the unorganised state of fishing and hunting to the carrying on of cattle-rearing, and finally to that of a permanent state of agriculture, could naturally take place but slowly, since it was often interrupted by feuds, wars of aggression, and destructive natural events. During this progress there was naturally an increase in the amount of capital and a greater division of labour. The products of human industry increased in number, so that at first the individual families, and gradually whole districts, were at length dependent upon the exchange of their commodities. Not only agriculture became localised, but towns arose first as places of protection against the wandering hunters and nomadic tribes. Behind their walls industry began to develop. The progress of agriculture could happen but slowly. Division of labour extended more and more, and people endeavoured to become more completely independent of Nature. With the development of industry in towns, commerce gradually attained moderate proportions.

The progress in technique rendered products more manifold, and thus made trade more necessary and profitable, so that later on



It was destined to become an independent branch, whereas formerly producers and consumers had themselves performed the exchange of their goods. The progress of navigation enlarged the area of commerce and rendered the people more independent of the slow, difficult, and expensive transport by land. Coined money, which only gradually replaced the less perfect means of exchange, facilitated the circulation of values. The same was effected by credit, which also could only gradually become influential with the progressive establishment of legal rights. All economic factors were strengthened by alternating influences. So at last we come to the times when history, no longer based upon supposition but upon fact, begins to make record of more extensive business relations; up to the close of ancient history there appears a series of great nations, each with its peculiar circumstances and fortunes. These nations were Egypt, India, Babylonia, Persia, Phoenicia, Greece, Carthage, and Rome.

**THE COMMERCE OF ANTIQUITY.**—Nearly three thousand years before the Christian era, the *Egyptians* had already attained a high degree of civilisation, which is testified by the existence of the Pyramids. Enclosed in a valley of about 500 miles in length, but confined to the region of the Nile on an area of a few square miles, they were not acquainted with the sea, and their caste system was opposed to commercial intercourse. Under the New Empire, dating from about 1600 B.C., they were in contact with Phoenicia, Syria, and the borders of the Red Sea by means of the caravans, which brought them spices, balm, and myrrh; and at a later period, about 600 B.C., Greek merchants visited Egypt.

Mesopotamia was an agricultural valley of great fertility, which required metals and raw materials. From Arabia on the south, from Syria on the north-west, and from Persia on the east, precious metals, cereals, wool, and building materials were taken to Babylon (which was then a busy market centre) as early as 3000 B.C.

The *Assyrians* extended their domination over Babylon, Armenia, Syria, a part of Irania, and over Palestine, and merchants could with safety resort to Nineveh.

The *Persian Empire*, which succeeded it, extended from the Mediterranean to the Indus, from the Indian Ocean to the Black Sea, and to the Caspian Sea, and thus covered a larger area than half of modern Europe. Up to the time of its destruction by



Alexander in 330 B.C., it commanded the whole of the commerce with the East, although its importance must not be unduly exaggerated. With respect to the Jews, they were then a pastoral and agricultural people, and could not be considered as traders.

Restricted to a strip of territory of about 20 miles in breadth and about 200 miles in length, the *Phoenicians* were separated from Syria and Palestine by mountain forests, but were always desirous of making exchanges with others. In prehistoric times they had formed a federation of self-governing cities, of which Sidon and Tyre were the most important. The majority of these towns should have been ruled by kings, but their power was limited by priests and magistrates. This form of organisation was naturally weak, and thus gave the people an impulse for expansion, and assured for them a maritime and commercial preponderance which lasted for about a thousand years. In A.D. 332 they remained sufficiently powerful to offer the greatest resistance to Alexander. The Phoenicians despised political power, but always kept in view commercial gain. In 608 B.C., in co-operation with the Egyptians, they undertook the circumnavigation of Africa. They had early been in communication with the African coasts, and also with Arabia and India, which was then known as Ophir. From the last-mentioned region, they imported spices, ivory, precious stones, and ebony. The Phoenicians also worked silver, iron, and tin mines in Spain, to which country they went in search of wool and skins. In exchange for raw materials, they exchanged cloth, household utensils, ornaments, and glass-ware, and also exported wine to Egypt. By land, their principal trade was done with Babylon and Palmyra.

The Phoenicians colonised the Mediterranean, and have endowed modern nations with the alphabet ; but since they had no great conquering or warlike monarchs, they have left behind no great monuments to celebrate their military exploits.

*Carthage*, a Phoenician colony founded in the ninth century B.C., achieved considerable development. Its commerce extended from Malabar to Wales. Their ruling authorities formed a caste, and were so strict, that they forbade their citizens to learn Greek, and refused all rights of citizenship to outsiders, whilst the Romans naturalised their neighbours and threw open the Senate to them. When Carthage was destroyed by the Romans in 146 B.C., neither



its fleet nor its trade was replaced ; and so commerce, for a time, disappeared from the Mediterranean, being abandoned to pirates.

*Athens* was at the height of her maritime and commercial power between 443 B.C. and 429 B.C. It drew its supplies from the Ionic colonies, which were scattered in the Archipelago and in Asia Minor.

The *Romans*, although they despised labour and trade, did not fail to appreciate profit, and compelled their slaves to execute strenuous tasks which they themselves would not think of doing.

In the period of antiquity, the temples were places for the conduct of trade ; and advantage was taken of the religious festivals to hold fairs, for they offered a greater security to the trader.

**THE MIDDLE AGES : A.D. 476—A.D. 1453.**—The history of the commerce of the Middle Ages begins with the fall of the Western Roman Empire in A.D. 476, and terminates with the sacking of Constantinople by the Turks in 1453. The chief characteristics of this period are—

- (1) The leadership of the Roman church.
- (2) The importance of towns.
- (3) The absence of a national spirit.

The beginning of the period is marked by a great upheaval in Western Europe caused by the migration of the Germanic tribes. This upheaval involved the rise and fall of great and warlike tribes, and ended finally in the lasting superiority of the Franks and the establishment of the State of Charlemagne. A further significant feature of the Middle Ages was feudalism, which retained its economic and political importance for a long time.

**Influence of Christianity.** Christendom in the Middle Ages was not merely a political and religious power, but it also exerted great economic influence. In the first place, it broke down the ancient view of the natural inequality of man, and thus attacked the institution of slavery. After the terrible desolation consequent, morally, on the decay of the manners of the Roman world and, politically, on the migration of the time, Christianity taught the nation and the individual to begin again from the beginning with economic and spiritual culture. Once more, agriculture became the basis of prosperity and simplicity the guiding rule to the enjoyment of life. But Christianity was to accomplish still more. Its tendency to embrace the whole world rendered it an excellent



medium by which peoples could be united. It enhanced the freedom and the position of labour, enriched family life, and hence there was an increase in diligence and temperance. As an external power, Christianity was aided by the power of the Church. In its regulations there was much of economic significance, and especially important were those in reference to interest ; its views concerning true and false profit ; on usury and also on luxury.

**The Monasteries.** In the sphere of industry the monasteries were, in many respects, worthy of imitation. They carried on agriculture ; rendered fit for habitation regions which were desolate ; and were exemplary schools for wine and fruit cultivation, as well as for many other activities. In the vicinity of these monasteries, villages were always seen to arise.

**The Crusades.** The influence of the East on the West was a result of the Crusades, which once more brought mediaeval Christendom into touch with the Orient. By bringing into contact North, South, and East, the Crusades awakened new desires, and in this way production and transport were furthered. The products and technique of the Orient were transplanted into Europe ; navigation in the Mediterranean underwent greater activity ; and the whole outlook and operations of the West were enlarged. This was absolutely necessary, for at the end of the Middle Ages the economic conditions of England and other European countries were in a primitive and uncouth state.

**The Towns.** Whilst agriculture was depressed and carried on badly by serfs who were looked upon with contempt, and was indebted to the monasteries for its progress, in the rising towns there were already sown the seeds of a new era of freedom. The inhabitants of the towns, through their guilds, kept in check the feudal lords. Mediaeval towns took their rise in Italy, where, behind the walls of the towns, the inhabitants found protection against warlike robbers. Industrial, artistic, and scientific activities, as well as the accumulation of capital, could exist only where protection was afforded. Large monasteries and places of pilgrimage became market places. With their growing prosperity and consciousness of their power, the towns began to struggle for independence, so as to obtain the right of self-government and the administration of their own taxes. The consequences were that quarrels and disputes arose between the towns and the nobles.



Throughout the greater part of Europe there was no specific industry. Manufactured goods were limited to arms, clothing, and the simplest articles of household use. Clothing and household utensils were made by the families themselves, and a higher degree of skill was to be found only in the monasteries and on the estates of princes.

**The Gilds.** This condition of affairs lasted for many centuries. Improvement was but gradual, and was not occasioned until the rise of a greater number of towns where the gilds could flourish. The main object of the gilds was protection and assistance to their members for the welfare of trade. The rise of the gilds took place between the eleventh and thirteenth centuries. At first, only the most common trades were united into gilds, such as the clothmakers, linen-weavers, tailors, tanners, butchers, and bakers. With the increase of commerce and of luxury, the number of trading gilds was augmented. The union formed by the gilds was a very strong one, for in them were combined masters, journeymen} and apprentices. Each gild had its own regulations concerning the management of its own trade, the acceptance of new members, the number of journeymen and apprentices, the length of apprenticeship, and the number of working hours. For centuries the gilds retained an influence on industry.

**Means of Transport.** The means of transport were very unsatisfactory, especially the roads, and this rendered river navigation more important. With the prevailing political divisions of territory, it was convenient and necessary that merchants and trading centres with similar interests should form themselves into gilds or become members of the Hanseatic League, in order better to protect themselves and to further their mutual interests abroad. Markets and fairs were the chief centres of trade, and special privileges were often granted to the traders by kings, princes, and bishops. The authority of states and of cities was manifested in trade by the granting of charters and in the existence of manifold restrictions, such as tolls, which were levied at numerous points in a most irregular manner.

**Currency.** The money of exchange was very badly organised, the kinds of coins being innumerable. Counterfeiting was frequent, and the relative values of silver and gold were fluctuating and irregular. The business of exchanging money was, therefore,



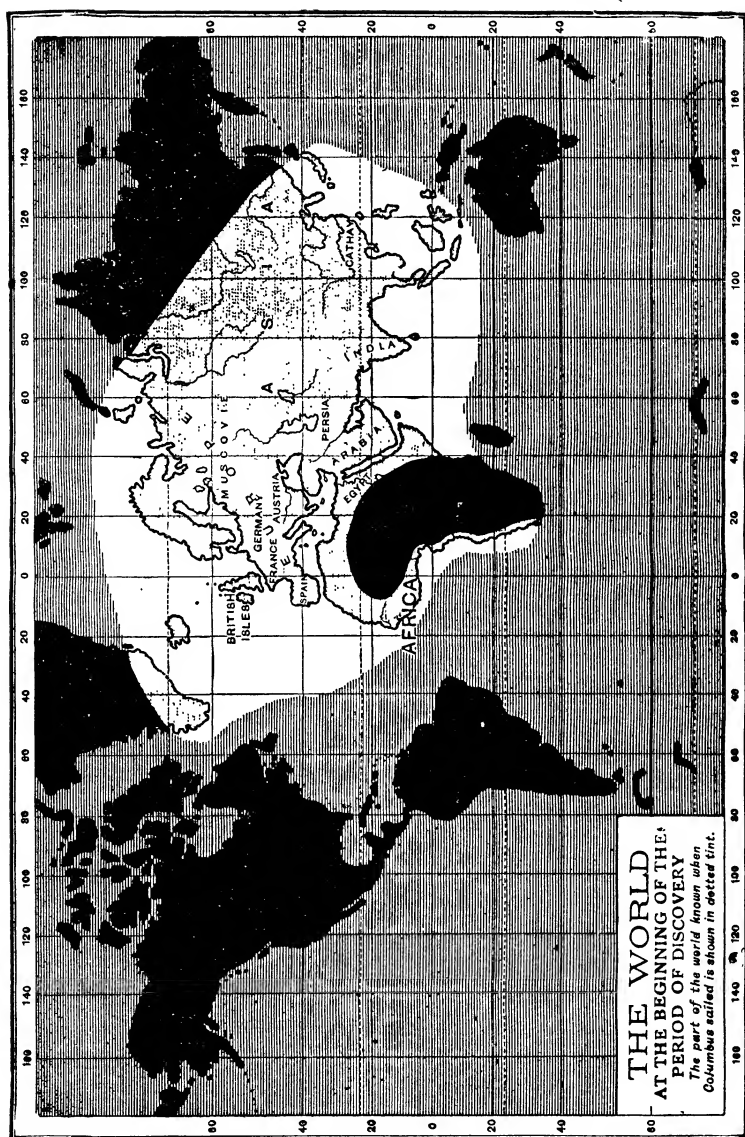
destined to become very lucrative, and was later carried on chiefly by the Italians. An important branch of their business was the issue of bank drafts. The payment by draft had been in vogue in the centres of trade along the Mediterranean since the thirteenth century, and, considering the insecurity of transporting metal to distant lands, bills were indispensable. With their institution, there gradually arose a body of law relating to bills of exchange, for the development of which the Italian gilds were responsible.

**The Jews.** Although the Church was no friend to the receiver of interest and opposed the extension of credit by its prohibition, yet it became customary in commercial transactions, and all kinds of usurious practices were employed whereby the payment of interest was concealed. In this way, the rate of interest was maintained at a high but constantly varying rate. Throughout the whole of the Middle Ages the Jews held a peculiar position in the sphere of commerce. Excluded from agriculture and manual labour, they were compelled to turn their energies to trade. As the Christian prohibition against the taking of interest was no concern of theirs, the loan of money at interest became for them an extensive and profitable business. Exiled, robbed, and restricted by laws regarding usury, they were nevertheless resorted to by debtors, great and small, and in consequence became increasingly rich. The feeling of a common descent, and the sufferings they had experienced in common, became a strong tie which united the Jews of every nation, and in their mutual intercourse awakened a confidence which added greatly to the development of suitable conditions for credit.

**THE PERIOD OF DISCOVERY: 1453-1760.**—This period extends from the capture of Constantinople by the Turks in 1453 to the beginning of the Industrial Revolution in 1760.

Up to the end of the fifteenth century, the world's commerce moved in the same channels as had gradually been followed since the earliest times, being concentrated around the Mediterranean. Navigation was limited to the coasts; few new countries had been opened up, and many of the old spheres of trade had been lost sight of by the Europeans, especially since the Turkish conquests in Asia. Up to that time, throughout the course of commercial history, there had been but few events which, like torchlights, lit up the darkness in which half the world was then enveloped.







The chief of these were the voyages long since effected by the Phœnicians ; the journeys of the Arabs to the Indian and African coasts in search of trade ; and the daring voyage of the Normans at the beginning of the eleventh century via Greenland to the east coast of North America, which was then known as Vineland. Starting from Iceland, they discovered Greenland ; and the seafaring adventurers, Björn and Leip, in 1001, reached the coasts of Labrador, Massachusetts, and New York, calling them by the name of Vineland.

The expeditions to these parts were repeated by other adventurers (e.g., by Markland in 1347) ; the discovery, however, was not pursued systematically, for the compass was not yet used whereby the open ocean could be penetrated, so that the trading routes remained the same. A more important event not sufficiently emphasised in commercial history, which led to a considerable transformation in the conduct of commerce, was the ability to sail across the sea against the winds : to the Norman seamen this had been unknown.

On the other hand, but little, if any, progress had been made in the improvement of inland trading routes. Even the journeys of the great Marco Polo were not imitated, and could not be followed when once Islam had set its foot firmly in Asia. Then there proceeded from a small seafaring nation, in the far west of Europe, the impetus to the mightiest transformation ever experienced in the world's commerce.

It was as a mere phantom in the minds of all seafaring men that behind the known seas, behind the dreaded ocean, there might lie other lands. Stronger and stronger became the clues that were advanced, and to these were added the reminiscences of old tales of sea-adventures. Through the agency of the Arabs and the Asiatic caravans, there came again and again the precious goods of India, and the reports of the fabulous wealth and beauty of that land. All these produced a powerful desire to penetrate behind the narrow borders of the known world.

**Remarkable Discoveries.** The credit of opening up new and important routes to the world's commerce belongs to the Portuguese. In 1415, the Infant Henry the Navigator, incited by geographical researches, equipped his first expedition to the West Coast of Africa, after which there began a period of the most remarkable discoveries.



This expedition, however, only reached Cape Bojador ; four years later, however, Porto Santo and Madeira were discovered, followed in short succession by the green headland and the coasts of Guinea. The rare and valuable goods which the navigators brought back with them awakened the thirst after adventure and the desire for gain, and consequently new expeditions set out for the South. The special end in view was the discovery of a sea-route to India. This became of increasing importance after the sacking of Constantinople by the Turks in 1453, since they intercepted trade with the East.

In 1475 the Equator was crossed, and in 1487 the enterprising Bartholomew Diaz reached the Cape.

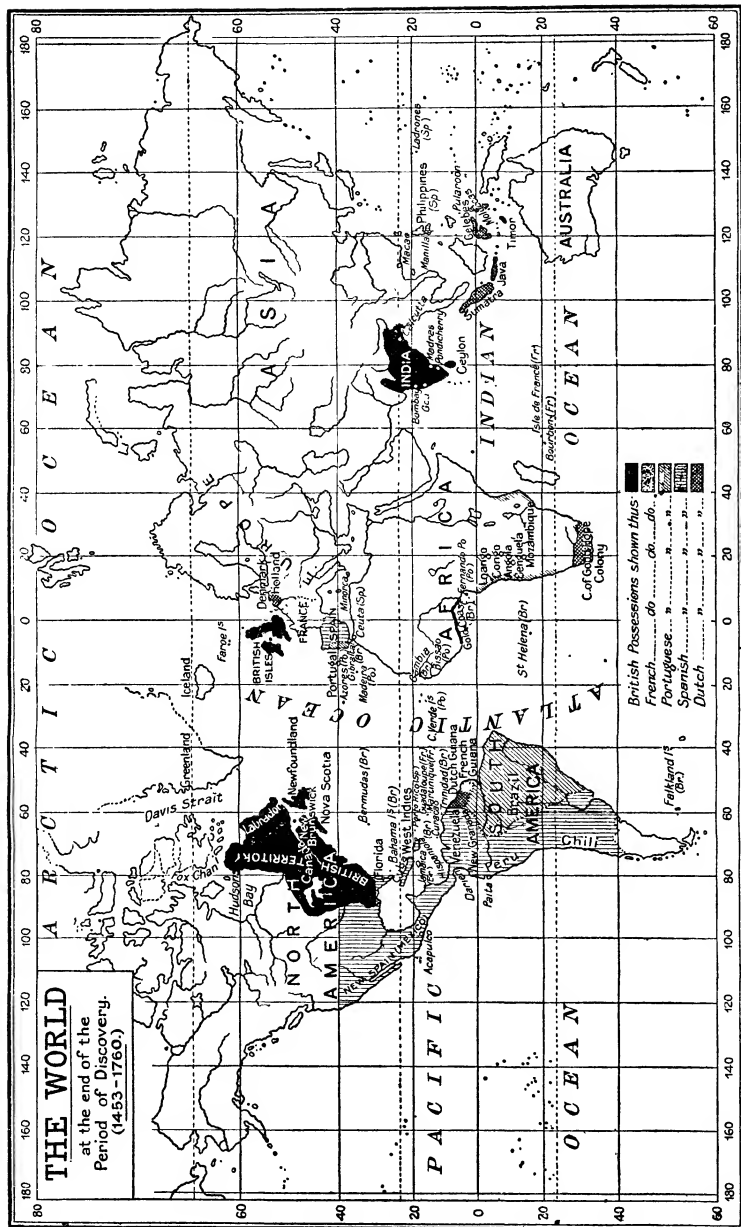
In 1497, Vasco da Gama succeeded in rounding the Cape, sailing north along the East Coast of Africa, and with the aid of an Arabian pilot cut through the Indian Ocean ; and on the 20th May, 1498, landed in Calicut on the coast of Malabar. The sea-route to India was thus discovered. A few years later, namely, in 1500, Cabral, under the orders of his king, after having discovered Brazil, obtained a temporary footing in India. It was not until the administration of Admiral Almeida, and afterwards under the great Governor Albuquerque, that the Portuguese could maintain a permanent footing in India.

Almost simultaneously with the discovery of the sea-route to India, an event of still greater significance took place. The Genoese sailor, Christopher Columbus, little esteemed by his own country, found a willing hearer of his ambitious schemes in the person of Queen Isabella of Spain. To discover a new route to India, he set sail from Port Palos with a small squadron of inferior ships to cross the Atlantic Ocean in nine weeks, landing on the 12th October, 1492, on the island of Guanahani in the West Indies. On the same voyage, Cuba and Hayti were afterwards discovered ; and, on later voyages, the remainder of the West Indian Islands ; and, finally, the mainland of South America. Columbus died under the misapprehension that he had discovered the eastern coasts of China and Japan.

In 1512, the Spaniards landing at Florida discovered the North American Continent ; soon afterwards, Vasco de Balboa made his way across the Isthmus of Darien to the South Sea. The daring Cabot, who had already, in 1497, when sailing from Bristol,



at the end of the  
Period of Discovery.  
(1453-1760.)





sighted the mainland of North America, explored as far north as Hudson Bay in 1517.

In 1519, Ferdinand Cortez conquered Mexico ; and in the same year, the Portuguese Magellan commenced his tour round the world in Spanish ships. Rounding the southern point of the New Continent, he discovered the Australian group of islands known as the Ladrones and the Philippines, and his ship at last returned to Spain in 1522.

When, in 1531, Francis Pizarro had conquered Peru, the most daring events of the age of discovery had been performed. But discoveries were by no means at an end. The English circumnavigated the North Cape to Archangel in 1523 ; the Dutch penetrated as far as Spitzbergen in 1595, and the Englishman Hudson discovered the most important parts of North America in 1607. The circumnavigator, Francis Drake, sailed from the southern point of America, along its western coast as far as the Oregon. In the seventeenth century there also began the discovery of Australia and the islands of the Pacific by the Dutch and the English. Thus from the end of the fifteenth century onwards, many new seas and lands were opened up. A completely new continent had been discovered : Portuguese and Spaniards, Dutch and English, became, in succession and simultaneously, sea-faring conquerors. The result was that many of the old trading routes were discarded, and the commerce of the world was undertaken by new towns and peoples. The centre of gravity of the world's trade passed from the East of Europe to the Atlantic coasts. Indian goods were poured into Europe in larger quantities and at a cheaper rate than formerly.

**New Commodities.** From the period of discovery onwards, there was a great increase in the quantities of goods imported, and also the introduction of many new commodities. These became not merely the source of much speculation, but gradually took their place as articles of general consumption, and in this respect helped to transform the mode of living in European countries.

The *Sugar Cane*, indigenous to the plains of India, and already known in the Middle Ages, became, in the sixteenth century, an important article of commerce, being principally derived from the Levant and from Spain. Having been planted in San Domingo



as early as 1520, it was introduced into Cuba, and shortly afterwards the West Indies became the chief centre of production. Later, North America, Brazil, Mauritius, and Bourbon became important sources of supply.

*Coffee*, indigenous to East Africa, and known from time immemorial as a beverage in Ethiopia, was cultivated widely in Arabia from the fifteenth century. It was unknown in the Middle Ages to Europeans, but was exported in the sixteenth century from Arabia to Egypt and Constantinople, and was in favour among consumers throughout the Levant in the seventeenth century. Coffee-houses already existed in Cairo in the sixteenth century. Coffee was enjoyed in Europe from the middle of the seventeenth century, but only by the wealthy classes. It was transplanted from Arabia by the Dutch to Java in 1650; it was introduced into the West Indies by the French, and its cultivation soon spread throughout the tropical regions of the Old and New World to Ceylon, Surinam, New Guinea, Brazil, etc.

*Tea*, which was first brought to Europe by the Dutch and Portuguese towards the end of the sixteenth century, was consumed only in small quantities up to the eighteenth century. Its use became general in England, and then spread to the Continent. The transplantation of the tea-plant did not take place so extensively as that of the coffee plant. Its plantation in South America, for example, proved unsuccessful.

*Cacao*, with which the Spaniards had become acquainted in Mexico, soon found an active sale in Spain and Italy. Later, it was also transplanted to the West Indies, South America, and Java.

*Tobacco* was in all probability brought by the Portuguese from Brazil, and at first used as a means of decoration and for medicinal purposes, until the English colonists in North America had learned to smoke, and the custom was introduced into Europe by sailors and soldiers about 1586, where, in spite of early opposition, it remained as a permanent institution. The cultivation of tobacco began to flourish in the British Colonies of North America, and especially in Virginia as early as 1616. When the Mohammedans became acquainted with tobacco, it soon formed a general means of enjoyment throughout the Islamic world, and its plantation spread over the Levant, Persia, and India.

The *Indigo* plant, known in Europe since the time of the



Crusades, was for long used in but small quantities. From the seventeenth century onwards, however, indigo began to supplant woad, in spite of the opposition of the woad-growers. India remained the chief source of supply, but it was also successfully planted in Central America and Egypt.

The *potato*, which was brought from America to Ireland by Sir Walter Raleigh, was indigenous to the South American Cordilleras, and spread slowly but under great difficulties, having at times to be secretly or forcibly introduced. Its general cultivation in Europe dates from the second half of the seventeenth century.

It was during this period that the Dutch established a monopoly in the Corn Trade. They procured their supplies from Dantzic, and from 1619 the Corn Exchange of Amsterdam became important for the European trade. With regard to the corn trade in other countries, a careful administration was exercised, and the trade was curtailed by prohibitions and duties. During the eighteenth century, Southern Russia and America also became sources of supply.

**The Slave Trade.** The most regrettable branch of the world's trade was the slave trade. From the Period of Discovery, the Portuguese had already engaged in it; and in Portugal, as in Spain, slave markets existed about the year 1460. Soon after the discovery of America, African slaves were brought here, and slavery spread from the West Indies to the American Continent. The trade grew in importance when the advantage of using the strong negroes in place of the weak natives was pointed out in 1517. The negroes were at first brought to Hayti, and afterwards to the remainder of the West Indies. In spite of the opposition of several Popes, the slave trade continued to increase, and the warning given by many far-seeing statesmen that slavery would be an economic and political danger to the Colonies was ignored. The profit was too attractive, and the strong negroes alone could be successfully employed in the West Indian plantations.

Nearly all European nations began to deal in human beings—the Portuguese, Spaniards, French, English, Germans, Danes, and Swedes. The negroes were stolen not merely from the coasts, but from the interior regions of Africa. Slave traders found markets not only in the West Indies, but also in the English colonies of



North America. At first, the principal traders were the Portuguese and, after them, the Dutch. The Spaniards themselves had not dealt in slaves since the sixteenth century, but they allowed other nations to bring the slaves into their colonies. In the reign of Queen Elizabeth, the English became ardent slave dealers, and Liverpool was especially enriched through this trade. Not until the second half of the eighteenth century did the anti-slavery movement gain ground; and then on account of the growing influence of the Press and the increased power of the people, the traffic was rendered illegal.

**The Mercantile System.** A characteristic feature of this period, as compared with the Middle Ages, was the formation of great States which were nationally administered, and the strengthening of the central Government as compared with that of the towns or guilds. These circumstances led to the economic conditions of the guilds and towns developing into State control. From this is to be explained the rise of an economic system as applied to the State, which exercised its influence for centuries. Through this system of State administration, many long-standing and local peculiarities were improved, and a wider view was substituted for many of the restricted ideas which prevailed. Instead of individual towns as formerly, the nations now began an active conflict for their economic existence. Trade, manufactures, and transport were subject to the growing power of the State. In the sphere of economic life those principles began to develop, which were afterwards known collectively as Mercantilism—a system which, by means of financial and administrative arrangements, aimed at directing the whole economic state into certain definite channels. According to the Mercantilists, the prosperity of a nation is determined by the quantity of gold in the country, and the whole of the economic system should be so arranged as to draw into and keep in the country as much money as possible, and to send out as little of it as possible. Therefore, every branch of industry in a country should be developed so that goods need not be imported, but may be exported. The difference between the exports and the imports must then be paid for by other countries in money. This difference is the so-called *Balance of Trade*, which was said to be favourable if the exports exceeded the imports and if the export of gold was less than the amount imported.



In order to obtain a favourable Balance of Trade, the Government had to prohibit the importation of foreign goods by means of the imposition of duties and the prohibitions of imports ; and at the same time it also aimed at rendering more difficult the exportation of raw materials grown at home, as well as the exportation of gold and silver. On the other hand, every facility was given to the export of home manufactures. The objects of the system may be summarised as follows—

### THE MERCANTILE SYSTEM

<b>The Mercantile System</b>	<b>I. Restraints on Importation</b>	{	(a) From any country of goods that could be produced at home.	
			(b) Of any kind of goods from countries that were importing English gold.	
	<b>II. Encouragements of Exportation by</b>	{	(a) Drawbacks	(i) From Excised Goods
				(ii) From re-exported Goods
			(b) Bounties	
			(c) Commercial Treaties	
		(d) Colony Monopolies.		

Up to the time of the Industrial Revolution, this system was predominant in England, having lasted from the Period of the Middle Ages. It was firmly established by Oliver Cromwell in the seventeenth century, in the form of the Navigation Acts ; and, in France, by the French Minister, Colbert. The latter, in particular, endeavoured to put the system into operation in almost every detail. In Germany, the founder of the Mercantile System was Charles V ; and other countries followed, until throughout the whole world the mercantile idea of the supreme value of gold prevailed. In Russia, the system flourished from the time of Peter the Great, and was still in operation at the beginning of the nineteenth century.

### IMPORTANT DATES IN EARLY COMMERCE

1280—1760

- 1280. Invention of Gunpowder by Roger Bacon.
- 1302. Mariner's Compass invented by an Italian, Flavio Gioja.
- 1348-9. The Black Death.
- 1381. Navigation Act which assisted the English carrying trade.
- 1407. Merchant Adventurers Trading Company formed, which superseded the Hanseatic League.



- 1440. Invention of Printing by Gutenberg.
- 1476. Printing introduced into England by Wm. Caxton.
- 1492. Discovery of America by Columbus.
- 1497. Discovery of the Cape Route to the East by Vasco da Gama.
- 1581. Levant Company formed.
- 1600. East India Company formed.
- 1606. Virginia, first successful British Colony established in North America.
- 1651. Navigation Act.
- 1660. Navigation Act.
- 1694. Foundation of the Bank of England.
- 1696. Formation of the Board of Trade.
- 1783. Kay's Flying Shuttle invented.
- 1757. Clive conquers Bengal—beginning of British territorial power in India.

### TEST PAPER XII

1. Enumerate the chief nations which experienced their rise and fall during the Period of Antiquity.
2. Name the most important commercial and maritime nation of ancient times, and say what you know of it.
3. Say what you know of Carthage, Assyria, Mesopotamia, and Egypt.
4. When does Ancient Commerce end and Mediaeval Commerce begin? Give reasons for your answer.
5. Outline the chief characteristics of the Middle Ages.
6. Trace the influence of Christianity upon the early development of Commerce.
7. Estimate the influence of the monasteries and the Crusades upon the development of commerce and industry.
8. Account for the origin of town life and of the craft guilds during the Middle Ages.
9. What was the object of the Hanseatic League?
10. Why did the Jews play so important a part in the commerce of the Middle Ages?
11. Give a description of the world at the beginning of the Period of Discovery.
12. State the chief discoveries which took place during the fifteenth and sixteenth centuries.
13. Mention the nations which took a prominent part in the trans-plantation of commerce from the Mediterranean to the Atlantic.
14. What were the chief results of the discovery of America and the Cape route to the East?
15. Say what you know of the introduction of sugar, coffee, tea, tobacco, and indigo into Europe.
16. Which was the most regrettable branch of the world's trade during the sixteenth and seventeenth centuries?
17. Explain carefully the meaning of the Mercantile System and criticise its defects.
18. "Mercantilism, in its innermost kernel, was nothing but State-making—State-making in the modern sense, which creates out of the political community an economic community." Criticise this statement.



## CHAPTER XIII

### THE MODERN HISTORY OF COMMERCE

MODERN commerce may be said to date from the time when steam was applied to machinery, and thus gave rise to the system of industry on a large scale. Six periods may be distinguished—

- (1) The Industrial Revolution, 1760–1820.
- (2) The Period of Free Trade, 1820–1870.
- (3) Period of International Rivalry, 1870–1914.
- (4) First World War, 1914–1918.
- (5) Period of Peace and Recovery, 1919–1939.
- (6) Second World War, 1939–

**THE INDUSTRIAL REVOLUTION : 1760-1820.**—The phrase “ Industrial Revolution ” seems to have been the invention of Mr. Arnold Toynbee, and was applied by him to a series of conspicuous changes which occurred in the aspect of British industry, and afterwards spread over the whole of the civilised world. This series of changes coincided roughly with the period from 1760–1820 ; and, taken collectively, they certainly do indicate a vast and comparatively sudden alteration in industrial conditions, a vast and sudden increase in man’s comprehension of Nature, and, therefore, in man’s power to control natural forces.

The word “ Revolution ” as applied to these changes can scarcely be said to be well chosen. The changes, it is true, were great, and it is the magnitude of those changes that has justified the application of the word “ Revolution,” and has since secured the acceptance of the term by economists. But, in reality, these changes no more constituted a revolution in the proper sense of the word than the opening of the rose-bud into the rose. It was a development—a growth, perhaps—partaking of the nature of what is known in biology as metamorphosis, but nothing of a revolution in the truest sense.

The transformation, great as it was, which took place during these years was far from being the first in time. Man had undergone far more fundamental changes in his organisation long before this ; in the organisation, that is to say, by which he has endeavoured to satisfy his wants. The greater landmarks of such change, beginning very far back in man’s history, are—

- (1) The separation of employments whereby man passes from working



for himself alone to exercising his individual skill for the benefit of his fellow-man—i.e., for mutual aid. That change possibly marks the transition from what is known in Geology as the Old Age of Stone to the New Age of Stone, or from the Paleolithic to the Neolithic Man. Paleolithic man has left remains of his flint tools and implements; but, so far as can be seen, there was no place in this Old Stone Age where tools were made. The individual man made an individual flint axe for himself, and with its service to himself was satisfied. But in the Newer Age of Stone—the age of the cave-dwellers—long before man discovered the secret of metals, there was to be found an accumulation of chips where the flint implements had been made. A workshop is a place where man works not for himself but for others, and here is the first evidence of the existence of such a place. This separation of employments built on the gift of skill—one man being able to do one task better than another—marks the first great change when man passes from a solitary animal to a social human being, and is, perhaps, sufficiently great to be termed a “Revolution.”

(2) The change from hunter to nomad; the change from the tribe that knew nothing of an animal except that it was to be pursued, its flesh eaten, and its skin fashioned into garments, into that of the patriarchal condition of the Old Testament. Flocks and herds were domesticated for man's use, instead of hunted down and destroyed.

(3) The next change is from the nomadic to the agricultural or settled state. Man is no longer a mere wanderer from pasture to pasture, but now settles in one place and, by cultivation, forces the earth to yield him continuous sustenance. There was a gradual development leading from the patriarchal institutions such as are described in the ancient classics to feudal and aristocratic institutions of our own Middle Ages.

(4) Another great change has passed man on from agriculture to commerce; whilst,

(5) There is a change from commerce, which is largely agricultural, to manufactures, and our institutions correspondingly tend to become more democratic. So that the “Industrial Revolution” is by no means without parallel, nor is it without precedent.

**England in 1760.** A survey of England in 1760 would have shown that its industries were being carried on by methods that are best described as “still surviving”: that is, they were methods that were dying out, but they were just then still in existence.

The great changes that were to come were due to the fact that about this period the new methods were asserting themselves, and the adoption of new industries rather than the development of old industries marks the period. Up to the time of Elizabeth, what was called “cotton” had been a sort of woollen cloth, and it is remarkable that Adam Smith only mentions the word “cotton” once in his *Wealth of Nations*. It was in 1760 that the fly-shuttle, which was the first attempt at weaving machinery, was applied to cotton weaving; and in 1769 Arkwright patented his spinning roller, which was known as the spinning “jenny.”

Mr. Bains, the historian of the cotton industry, says that the English cotton machinery was absolutely primitive at this period,



and was the same to all intents and purposes as that in India. It was worked in the homes of the people in the forms of industry known as the "Domestic System." Under this system, the employer gave out the material to be worked up in the homes of the people where they possessed a loom or a spinning-wheel. Hence, the period begins with invention.

The great inventions, which, when once born into the world, were to grow with a mighty growth—were to constitute the large-scale industry.

By 1777, there were indications of the change. There were riots in Somersetshire against the owners of machinery. At the beginning of the eighteenth century, wages were settled by magistrates, but that system of fixing wages was dying rapidly in 1747; and by 1760 it was here and there surviving. By 1795, however, the system had been abolished.

The *population* in 1760 cannot be ascertained exactly, but estimates have been made by more or less skilful observers. One such estimate made by a Mr. Finlayson states that from 1700 to 1750 there was an increase from a little over five millions to a little over six millions, or from 17 to 18 per cent in the first half of the eighteenth century.

In 1801 there had been an increase to over nine millions, that is to say, more than 52 per cent in the second half of the eighteenth century; and the change marks the difference between the results of the old industrial organisation and the new. More striking even than the quantity of the population, was the change in its local distribution.

At the beginning of the eighteenth century, England, north of the Trent, was very sparsely populated indeed; but by 1801 it contained one-third of the vastly increased total.

Between 1700 and 1750, for instance, there was an enormous increase in Lancashire, in the West Riding of Yorkshire, Somersetshire, and Wiltshire, and especially in those districts where the textile industries were developing. Among the increases were—

NORWICH . . .	30 per cent.	BIRMINGHAM .	Sevenfold
WORCESTER .	50 „	LIVERPOOL .	Tenfold
SHEFFIELD .	Sevenfold		

Where trade and manufactures were closely connected, the



population seemed to advance by rushes. Again, the towns were absorbing an increasing proportion of this population.

It is estimated that in 1696 London contained about one-tenth of the whole population, whereas in 1766 London contained one-sixth of the whole. These figures point to a conspicuous change.

**Trade and Manufactures.** In 1760 the woollen trade was still the principal industrial interest, and was distributed fairly evenly over the country ; and the demand for wool led to the demand for sheep-runs. Next in importance after wool stood iron, which was then carried on as a decaying industry surviving in the Weald of Sussex and along the North Downs.

It was in 1755 that iron and coal works were first started at Merthyr Tydvil.

In 1760 the manufacture of cotton was quite insignificant, the production of wool being twenty times as great.

At the present time the production of cotton goods is three times that of wool. The chief centres of cotton manufacture were chiefly Bolton and Manchester in Lancashire, where the temperate climate was remarkably well suited to the production of cotton goods.

It was in 1760 that the fly-shuttle began to be used in Lancashire ; then came the development of the larger market, with its division of labour. Prices then became lowered, and this, in turn, gave rise to a still wider market. The prosperity of the towns began to influence the country, and the land was being bought up in large quantities by rich men, so that the yeomen gradually vanished. They had been gradually disappearing down to the year 1700, but up to that time they represented about one-sixth of the population of England. The causes of the disappearance of the yeomen were social and political, rather than economic. Land was the source of political power, and the poor man could not resist the rich man's price.

This transition from the old form of industry to the large-scale machine production was marked by a series of important inventions.

In 1767, Hargreaves invented his " spinning jenny " ; in 1769, Arkwright his cotton-spinning machine ; in 1788, Cartwright the first mechanical weaving loom. The invention of the steam-engine by James Watt in 1763 brought with it a complete transformation



in almost every branch of industry. Through the practical utilisation of this and numerous other inventions and discoveries, English industry was enabled to outdistance all competitors.

**Agriculture.** The changes which were taking place in agriculture during this period are often referred to as the Agrarian Revolution. The period was characterised by a great deal of enclosure of land. In England, there have been three great periods of *land enclosure*, but never before had land been enclosed with such rapidity or to such an extent as during this period of the Industrial Revolution.

The first group of enclosures was in early Feudal times, and received its sanction from such statutes as the Statute of Merton, 1226, and the Statute of Westminster in 1285. The Statute of Merton allowed the lord to enclose the land, provided he left sufficient waste for the tenantry. These early enclosures were, for the most part, only re-arrangements of estates, and conversions from wood and waste into arable land. In those times, it was the arable land which gave most employment to the people, so that the change caused very little grievance and the enclosed land was much superior to the so-called champion or open-field land.

The second great period of enclosure followed on the Black Death in the fourteenth century. It lasted from the reign of Henry VII at the end of the fifteenth century to the reign of Queen Elizabeth. It consisted of the conversion of arable to pasture land, and had disastrous effects.

The land which had formerly maintained whole villages was now converted into pasture, which maintained a shepherd and his dog. It was the answer of the Lords to the Peasants' Revolt.

The *enclosures* of the eighteenth and early nineteenth centuries were on a different principle, and led to the conversion of common land into private property, largely by means of Acts of Parliament. The causes of this movement were—

(a) The absence of all labour-saving machinery in agriculture, the development of large-scale farming, and the increased application of division of labour.

(b) The displacement of the small yeoman farmer, who sank largely to the level of the farm labourer, and, in consequence, led to the diminution in the price of labour.

(c) The increase in the number of private Enclosure Acts. In the reign of Anne, there were only three private Acts passed for enclosures; whilst from 1797 to 1810 there were 1,729 such Acts.

In 1856, commissioners were appointed to check enclosures, and later an Act was passed to prohibit further enclosures, unless the Commissioners explicitly decided that they were for the public good.

From 1710 to 1760, there were about 335,000 acres of land



enclosed ; whilst from 1760 to 1843 it amounted to 7,000,000 acres. These changes had advantages as well as disadvantages. The common tillage had been exceedingly primitive, and it was the enclosures which brought about improvements. Agricultural invention had come very late ; and in 1760, the commencement of this period, the wooden ploughshare was still in use.

In 1760, the mercantile system of close and constant interference with trade and industry was still in existence, although the economic thought of the world was soon to be revolutionised by the publication of that wonderful work, *The Wealth of Nations*, in which Adam Smith, with a chain of resistless logic, revealed the unutterable weakness of the mercantile theory.

**Features of the Revolution.** The chief facts which emerged, and which constituted the Industrial Revolution, are as follows—

1. The great change of population in regard to both quantity and distribution.

2. The decline in the proportion of the population engaged in agriculture, and the shifting of the centre of gravity of the population from the Midlands to the manufacturing district of the North.

3. Great changes in agriculture itself. The destruction of the common-field system ; the enclosures of waste land and commons ; the growth of large farms and the rapid advance in the most scientific kinds of agriculture, particularly in the rotation of crops ; the introduction of the steam-plough : these changes produced an immense improvement in the productiveness of agriculture.

4. In manufactures, the domestic system gave way to the factory system.

5. The great increase in the means of communication : the first railway in 1830 taking the place of the canals.

6. The growth of large towns on the coal-fields.

7. The separation of the farmer and the labourer in agriculture, and the capitalist and the worker in the factory.

**PERIOD OF FREE TRADE : 1820-1870.**—In 1786 an attempt had been made to modify the rigidly protective legislation of the eighteenth century. In that year, Pitt concluded a commercial treaty with France, providing for large reductions of duties in both countries. But the treaty was swept away with the outbreak of the Napoleonic Wars, and accordingly the old system of Mercantilism was still in force in 1820.



The first important step, and in some respects the decisive step towards modifying it, was in 1824, under the policy of Huskisson. In that year, and again in 1825, great reductions were made in the duties on raw materials, while considerable reductions were also made in the duties on manufactured goods. The most sharply contested of the changes were in regard to silks, which had been completely prohibited, but were now admitted at a duty of 30 per cent. A considerable breach was thus made in the protective system.

In the decade from 1830 to 1840, the *Corn Laws* were the chief subject of contention. The great increase in population since the middle of the eighteenth century had made England a corn-importing country, especially with the rapid growth of manufactures in the early years of the nineteenth century.

The first systematic Corn Laws, imposing duties on grain, had been passed in 1773. From 1816 onwards, a series of measures was passed, all designated to maintain the high price of grain. The Act of 1816 prohibited the importation of wheat, when the price was less than 80s. a quarter. In 1822, the prohibitive point was lowered to 70s.

In 1822 the *sliding scale* was introduced, under which the duty went up and down as the price of grain went up and down, and it was against this form of the Corn Law that the great agitation (led by Cobden and Bright) was directed after 1830.

For a long time the anti-Corn Law agitation seemed to have no effect, although conducted with extraordinary skill and enthusiasm.

In 1842, however, Sir Robert Peel made the first important concession, by modifying the sliding scale, his opponent, Lord John Russell, having proposed in the previous year a fixed duty of 8s. a quarter.

In view of the bad harvest of 1845-6 and the famine in Ireland in 1846, Peel surrendered; and proposed, in 1846, the admission of grain, with only a fixed duty of 1s. a quarter as a registration fee. This change was carried, but Peel, being able to carry only a fraction of his party with him, was compelled shortly afterwards to resign. The Corn Laws had great political strength, serving as they did the interests of the landowners, whose hold on Parliament was still very strong; but the general economic situation in Great Britain, from the rapid growth of the manufacturing population



and the imperative need of more food, made their abolition inevitable. The remodelling of the tariff system in the direction of Free Trade went on, little retarded by the maintenance of the Corn Laws and not much accelerated by their abolition.

In 1842 great reductions of duty were made on a large number of articles; in 1846 still further reductions of duty were made, whilst another series of changes came in 1853; and, finally, in 1860, the last remnant of protective duties disappeared.

The four Acts of 1842, 1846, 1853, and 1860—the first two under Peel's leadership, the second two under Gladstone's guidance—thus carried out the policy of Free Trade in regard to other articles than grain. The first of them, in 1842, was signalled by the introduction of the income tax as a means of raising revenue to replace that lost by the diminished import duties. The last of them, in 1860, was largely influenced by the great commercial treaty with France. In that treaty the concessions made to France were the reduction by Great Britain of duties on wines and spirits, and the admission, free of duty, of some important French products, notably silk manufactures, gloves, and other products in which the French had superiority.

Great Britain, instead of limiting the concessions to France in 1860, made them applicable to all the world. The silk manufacture, as to which the first great changes had been made in 1824, and on whose products the duties had been kept higher in previous Acts than on other manufactures, was thus compelled, notwithstanding violent opposition, to face unfettered foreign competition.

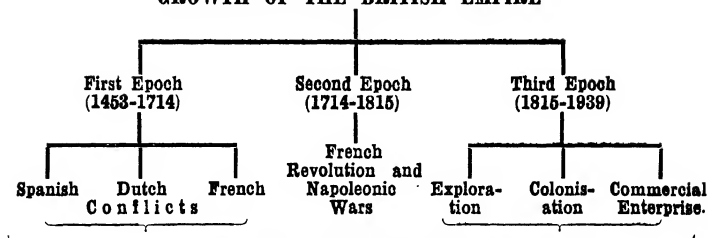
The nature of the changes effected between 1842 and 1860 is indicated in the following figures—

Year.	Duties reduced.	Duties abolished.
1842-46. . . .	503	390
1846. . . .	112	54
1853. . . .	—	123
1860. . . .	—	371

After 1860, only forty-eight articles remained subject to duty, a number which was still further reduced. From that date the



## GROWTH OF THE BRITISH EMPIRE



### Chief English Opponents

(1) Philip of Spain  
(Armada, 1588).

(2) Van Tromp defeated by Blake, 1653.

(3) The French Marshal Tallard, the Elector of Bavaria, and others, defeated by Marlborough.

(1) Dupleix and Surajah Dowlah, defeated by Clive in India.

(2) Montcalm, beaten by Wolfe at Quebec, 1759.

(3) Napoleon and his various generals, repulsed in Egypt, Austria, Russia, and overthrown by Wellington at Waterloo, 1815.

The Wars since 1815 have not aimed at Conquest or Expansion, but have been chiefly due to Exploration, Colonisation, and Commercial Rivalry.

### Leading Explorers, Colonisers, etc.

- (1) **THE CABOTS** discovered the mainland of North America, probably near Labrador.
- (2) **THE ELIZABETHAN ADVENTURERS**, especially Drake, who circumnavigated the Globe; Hawkins, who commenced the Slave Trade in America; Frobiisher, who attempted the North-west Passage; and Raleigh, who attempted the Colonisation of parts of America.
- (3) **CROMWELL**, who as Lord Protector initiated the vigorous foreign policy under which Blake destroyed the Dutch Power.
- (4) **CAPTAIN COOK**, the explorer, discoverer of Australia.
- (5) **WILLIAM PITT**, the Younger, whose offensive policy was especially directed against France, and which was carried out by—
  - (a) Clive and Hastings in India;
  - (b) Wolfe in America;
  - (c) Nelson at sea;
  - (d) Wellington in Spain.

The policy of Pitt outlived him, and eventually resulted in Napoleon's defeat at Waterloo.

- (6) **HAVELOCK**, **OUTRAM**, and others, whose efforts saved India at the time of the Mutiny.
- (7) **LORD ROBERTS**, in supreme command of British Forces in the Boer War.
- (8) **LLOYD GEORGE**, assisted by his War Cabinet, brought the Great War to a successful conclusion.

### Most Important Dates in Commonwealth Development

- 1588 Defeat of the Spanish Armada.
- 1653 Defeat of the Dutch in the North Sea.
- 1704 Gibraltar captured—route to the East secured.
- 1714 Peace of Utrecht—Nova Scotia ceded, right to trade in Southern Seas admitted.
- 1757 Battle of Plassey—Supremacy in India assured.
- 1759 Battle of Quebec—British North America ceded.
- 1763 Treaty of Paris—British North America and West Indies ceded.
- 1815 WATERLOO—England's right to her colonies definitely determined.
- 1857 Indian Mutiny—resulted in annexation.
- 1899 The South African War resulting in the Union of British South Africa.
- 1915 Kitchener's Army recruited from the Colonies and Dominions.
- 1924 British Empire Exhibition at Wembley.
- 1932 Imperial Economic Conference at Ottawa.
- 1939 Outbreak of Second World War.



English Customs tariff was simplicity itself. A very few articles, such as spirits, beer, wine, tobacco, tea, coffee, and cocoa yielded practically all of the Customs revenue; and so far as these articles were produced within the country, they were subject to an excise duty (i.e. an internal tax precisely equal to the import duty). Further, the advent of a pure Free Trade policy was accompanied in 1860 by the so-called Cobden Treaty between England and France, and was followed by a series of similar treaties with other countries, and there was a general movement throughout Europe for greater freedom of trade.

**PERIOD OF INTERNATIONAL RIVALRY: 1870-1914.**—The hope that other countries would follow England in the adoption of Free Trade was not to be realised, and from 1870 onwards a movement in favour of higher duties spread over the Continent; whilst, in England, the opposition to Free Trade once more came into evidence. The chief factor which gave rise to this reaction was the increasing competition in manufactures and in commerce on the part of the United States and of Germany.

In 1880 began a protectionist movement in England under the name of Fair Trade—the principle that a country should treat the products of other countries in the same manner as the latter treat its products. This agitation to abolish one-sided Free Trade was followed by various other measures against the existing *laissez-faire* system, such as the Merchandise Marks Act of 1897, which required the place of origin to be indicated on all imported goods. This was directed chiefly against German competition, although many believe that it had the unexpected effect of advertising goods “Made in Germany.” Further protectionist tendencies were manifested in the regulation of the importation of cattle, in the financial arrangements during the South African War, and more recently in the advocacy of Imperial Preference.

Although the trend towards combination started during this period, the dominant force in industry and commerce was still individualistic and competitive.

**FIRST WORLD WAR: 1914-1918.**—During the Great War the whole organisation and machinery of production were subjected to abnormal pressure under the driving force of government and necessity. There was immense speeding up of invention, technique, and organisation, leading to mass production over wide areas of industry.



During these years the government had to resort to extensive borrowing, with the result that there was a considerable rise in prices. At the same time the co-operation with the colonies led to the extension of Empire Unity. The Colonies received much benefit owing to the stopping of a great many European exports. Goods which many countries had obtained from Germany they now tried to produce for themselves, so that the War period was one of extensive factory building in British Colonies, and a Colonial industrial revolution may be said to have taken place at this time. British trade was hampered owing to submarines, and in 1915 duties were placed upon what were considered non-essential goods in order to discourage their import and thus have more vessels free to carry more important goods. A preference system with the colonies was further extended, and in 1917-1918 the Imperial War Conferences were held.

**PERIOD OF PEACE AND RECOVERY: 1919-1939.**—For some years after the first World War it was really doubtful whether Europe and Great Britain were recovering or were going to recover from these disastrous four years. Many thought that we were slipping downhill and would be unable to arrest our fall and that after a long period of distress, revolution and social disruption, the Europe which would emerge would be on a permanently lower level of prosperity and civilisation. Happily these darker fears for the future were not realised. European civilisation did, indeed, for a time totter in the balance, but when once the turn towards recovery was taken progress was surprisingly favourable. New inventions and increased skill enabled men with a given amount of effort to wrest more from nature and make more from her products. The war interrupted the growth of prosperity, but it did not permanently stop or reverse the process. In 1939 the world was richer than in 1914. Production had, since the war, increased by about 25 per cent, while the world population had increased only by about 10 per cent. The difference between these two figures indicates the real rise in the average standard of living. The world would have been, of course, much richer had there been no war; but in 1939 it had already grown richer than it was before the war. This of course is only true of the world as a whole; it is not true of every continent, still less of every country, still less of every class. In North America, in South America, in most of Asia, in Africa



and in all the British Dominions, in every continent except Europe, there had been rapid and striking progress. It was Europe which was impoverished by the war. For Europe the war meant, instead of increasing prosperity, a decade of impoverishment and then a slow resumption of progress up to the point reached in 1914. The position of our own country was rather worse. More than any other great country we depend, and must depend, on our export trade. We therefore suffered specially from the hindrances to world trade.

Let us glance rapidly at the principal stages in Britain's recovery\* and subsequent relapse into war. First we had the stage of emergency measures. Many countries were in 1919 short of the most elementary necessities. Food and raw materials had to be found in ships. There were not enough ships. Railways had to be repaired; the complicated restrictions of the blockade had to be cleared away; prisoners of war had to be repatriated; soldiers had to be demobilised and both reabsorbed in the occupations of peace. These troubles occupied the first few years of peace. Secondly, as progress was made in these tasks more obstinate difficulties emerged. The whole mechanism of production had been adapted to war needs; there was not enough savings to acquire the new capital and the large reparation debt was for years a serious obstacle to the resumption of trade. Closely connected with these troubles, and for a time the most important of all, came the chaos of the currencies of Europe. For some years the fluctuations of European currencies were the worst impediment to economic recovery and worst of all to the trade of large exporting countries like our own. In nearly all countries of Europe the currencies lost value and in many countries of Europe practically ceased to have any value at all. As this trouble passed another came into prominence. Trade barriers and new and increased tariffs were introduced, and the trade of the world was distorted and destroyed. Autarchy with its ideal of self-sufficiency became the economic ideal, whilst in the political sphere a policy of aggression was adopted by Japan, Germany, and Italy which soon led to the outbreak of the second world war.

**SECOND WORLD WAR: 1939.**—In September, 1939, war broke out once more between the British Empire and France on the one hand, and Germany on the other—a war which by the end of 1941 was to involve every Great Power in the world and to transform every continent into a battlefield. It would be hazardous to predict



the details of the social and economic organisation which will emerge from the struggle now raging. In the middle of 1941, however, a noteworthy pronouncement was made on the principles of the new world order to be established after the war. This was the *Atlantic Charter*, which aspired to guarantee for victors and vanquished alike access to raw materials and all the necessary conditions of a peaceful and prosperous life.

### TEST PAPER XIII

1. What was the "Industrial Revolution"? Point out the chief features of the change which came over the Industry of England at this time.

2. Justify the title "Industrial Revolution" as a description of the economic changes which passed over England at the close of the eighteenth and beginning of the nineteenth centuries.

3. Give an account of the organisation and diffusion of the woollen industry in England in the period immediately preceding the great mechanical inventions.

4. Describe and explain the general change in the nature of the manufacturing industry of England at the end of the eighteenth century.

5. "England in the Tudor Period is still primarily a country engaged in agriculture." What conditions gave rise to the subsequent development of manufactures and commerce?

6. Name four important inventions which have assisted in the growth of the British textile industries.

7. Account for the large number of enclosures at the end of the eighteenth and the beginning of the nineteenth centuries.

8. Describe the "Domestic System" of manufacture.

9. Point out the marked changes in the industrial methods, appliances, and means of communication of the nineteenth century, and describe the results of such changes.

10. Why has the England of 1800-1870 been termed "the workshop of the world"? Mention the chief inventions which made this term possible.

11. Indicate the nature of the financial reforms which took place in England between 1820 and 1870.

12. Account for the introduction of Free Trade into England.

13. What were the immediate effects of the introduction of Free Trade into England? What causes have led to the recent revival of the agitation for Protection?

14. Through what causes and in what respects has the industrial supremacy of Great Britain been impaired since 1870?

15. What are the chief factors you would take into account in estimating the economic progress of England during the last century?

16. Connect the progress of invention with the changes that have taken place in the local distribution of some of the chief English industries.

17. It has been said that Great Britain won an overseas Empire in the seventeenth and eighteenth centuries almost without knowing what had been done. Give some account of the way in which it was done.

18. Mention the names and describe the situation of the self-governing dominions of the British Empire. How did they come to be parts of that Empire and what other parts are there?

19. Name three outstanding events which have taken place in the commercial history of Great Britain since 1914, and give an account of *one* of them.

20. Would you prefer to be living now in the Great Britain of to-day or in the Great Britain of two or three centuries ago? State your reasons.



## IMPORTANT DATES IN MODERN COMMERCE

1760—1941

- 1760. Enclosure of Common Lands. More than six million acres were enclosed during the period of the Industrial Revolution.
- 1761. Bridgewater Canal opened.
- 1765. Hargreaves's Spinning Jenny invented.
- 1776. Adam Smith's "Wealth of Nations" published.
- 1783. Puddling and rolling processes for iron invented by Cort.
- 1789. Steam power used for working looms.
- 1802. First Factory Act passed.
- 1803. Steam-tug first used on the Forth and Clyde Canal.
- 1814. Geo. Stephenson constructs the first practical locomotive.
- 1815. Macadam and Telford revolutionise road-making and bridge-building.
- 1816. Great Britain adopts the Gold Standard.
- 1819. The Atlantic crossed by the S.S. "Savannah" from New York to London.
- 1825. Stockton and Darlington Railway opened.
- 1830. The "Rocket" locomotive run on the new Liverpool and Manchester Railway.
- 1837. The Electric Telegraph invented by Wheatstone and Cooke.
- 1839. Vulcanising process invented by an Englishman named Goodyear.
- 1840. Rowland Hill succeeds in effecting the establishment of a general Penny Post.
- 1846. Repeal of the Corn Laws.
- 1851. First Great International Exhibition held in London.
- 1853. Gladstone begins his Tariff Reforms.
- 1860. Gladstone completes the Free Trade system in England.
- 1865. Abolition of Slavery in America.
- 1869. Completion of the Suez Canal.
- 1889. The Forth Bridge constructed.
- 1896. Marconi invented Wireless Telegraphy.
- 1899. Outbreak of the Boer War.
- 1903. Russo-Japanese War.
- 1906. Grant of Responsible Government in South Africa.
- 1906. Commencement of the Conquest of the Air.
- 1914. Outbreak of the Great European War.
- 1914. Panama Canal opened for traffic.
- 1919. Peace concluded by the Treaty of Versailles.
- 1928. Kellogg Peace Pact signed by representatives of fifteen nations.
- 1931. Great Britain relinquishes the Gold Standard.
- 1934. Establishment of a regular weekly air mail service between England and Australia.
- 1939. Outbreak of Second World War.
- 1941. The Atlantic Charter.



## CHAPTER XIV

### THE ESTABLISHMENT OF A BUSINESS

BROADLY speaking, business concerns are founded with the following objects—

- I. To provide employment for Capital.
- II. To provide employment for Labour.
- III. To provide a supply of some particular commodity.

It will be noticed that the object of providing work for persons overlaps that of the provision of a supply of commodities, since the latter may consist of services. However, this classification is most convenient for our present purpose.

**I. EMPLOYMENT OF CAPITAL.**—Those who are in possession of capital are always anxious to find a profitable means of investment, and the fact that good profits can be made in any particular industry will always tend to attract capital in that particular direction. It is always easier to find capital for an industry which is known to be prospering than for an industry which is known to be in difficulties. The fact that any particular form of industry is known to be profitable tends to increase the amount of capital invested for the time being in that particular industry. This, in its turn, leads to an increased production, and ultimately, to over-production of commodities. The result is a curtailment of profits in consequence of the fall in prices and the diversion of capital from the industry, so that there follows a period of depression. This cyclical movement of prosperity and depression repeats itself *ad infinitum* in most industries, and is known as a Trade Cycle.

Apart from the waxing and waning of profits as a result of too much or too little capital being offered for use in that particular kind of industry, the influence of legislation is also important. Legislation may either encourage or restrict an industry, and may greatly affect the ease with which it can find capital. For example, the fact that a particular industry is protected in some countries by either tariffs or subsidies, and is not protected in other countries, will result in some cases in encouraging the investment of capital in the protected countries, because bigger profits are to be made by those who are within the ring fence of the protection.

There are three classes of persons who are engaged in directing the flow of capital into the most profitable industries, and who are



occupied in establishing a connection between those who have capital to invest and those desirous of finding employment for the capital of others. These are—

1. Company promoters.
2. Brokers.
3. Underwriters.

Bankers are not here included, since it is not a legitimate function of a banker to have capital permanently invested in an industry, but, rather, to lend money on short loans which can easily be recalled.

**Promoters.** A promoter is a person whose business it is to observe conditions, to find out those industries most in want of capital, and most capable of being developed by capital, and, therefore, most likely to be able to offer a sufficient inducement for the capitalist to part with his money. As a rule, the promoter does not act merely as a broker or agent, whose business is merely to introduce the parties, but he steps in between them as an independent middleman. He may purchase what he considers to be a likely undertaking and then dispose of it to a company, thus making a profit out of his deal.

In short, the company promoter is a trader in businesses or properties. He may trade in established businesses already making satisfactory profits and capable of being developed by the investment therein of an increased amount of capital; or he may deal in possibilities, as in the case of a mining company, where the district has only been prospected, but it is believed that it can be worked on a commercial basis.

**Brokers.** The broker is primarily the person responsible for finding the capital which is required by the promoter. The broker is a professional man acting as agent on commission for a great number of persons who, in varying degrees, have money to invest from time to time. Accordingly, a broker is in touch with a certain number of possible investors in any reasonable kind of enterprise. A broker may confine himself to a specialised kind of business; e.g. he may undertake to find capital solely for mining concerns, whilst another broker, with a much larger connection, might be unable to procure investors in such undertakings. The broker is able to bring the opportunity of a particular form of investment to the notice of his own particular *clientèle*. Many persons are prepared to listen to him much more attentively than to a stranger, and would prefer his advice to that received through the post in the form of an advertisement. In this way, he serves the useful function



of bringing together parties who are strangers to each other, but who may transact business to their mutual advantage. For these services. it is customary for the promoter to pay the broker a commission on any capital he is able to introduce. This commission is paid by the promoter out of his profit.

The broker also performs another function in connection with concerns which take the form of companies. This arises out of the peculiarities of companies themselves, under which the capital takes the form of shares, stocks, etc., which are capable of being sold. If the possessor of shares in a company is desirous of converting them into money, he does so through the medium of a broker, and accordingly it is the brokers as a body who are able to give to the capital of companies the quality of realisability. When an investor acquires shares in a company he usually assumes that he has acquired something which is capable of being sold, through the medium of a broker, in case of need, and it is in the hope and expectation that it will be so saleable that he is more willing to invest than he would otherwise be.

To establish that degree of saleability in the capital of a company, the promoter enlists the aid of a broker not merely as an introducer of capital but as someone who will afterwards act as the intermediary between those who hold capital and wish to realise it and those who wish to acquire holdings. For the purpose of establishing this degree of saleability in as perfect a form as possible, it is customary for companies to appoint brokers of their own ; that is to get one or more firms to allow their names to be put forward as brokers, thus emphasising the fact that the shares are going to be dealt in on the Stock Exchange. This has a beneficial effect in making it easy to get capital.

**Underwriters.** The underwriter is also a person who assists in the circulation of capital. His function is to guarantee to the promoter that at least a minimum amount of the capital which he is desirous of placing will be subscribed. Therefore, the underwriter really acts as insurer ; but the underwriting of capital is rather different from ordinary insurance business, and is usually carried on by a different class of persons. It is usually organised and negotiated by Stock Exchange men, who partly do it themselves and partly introduce clients of theirs who are willing to do it.

The underwriter, in consideration of being paid an agreed



commission, undertakes to subscribe a given amount of capital if the public fail to do so. For instance, suppose the promoter was desirous of obtaining a subscription of £50,000, he may enter into agreements with underwriters who, among them, guarantee that the subscription list shall not fall short of that amount. The extent to which the public subscriptions fall short of £50,000 must be made up by the underwriters themselves, the amount being divided *pro rata* according to the sums they have respectively underwritten. The underwriters receive their commission on the amounts they underwrite, whether or not they are afterwards called upon to take up any shares. If the issue goes well they get their commission and have nothing further to do with it. If the issue goes badly, they may have to apply for the full number of shares they have underwritten, and they would have to pay for them at their full face value. On the other hand, they receive full commission on the shares they underwrite, so that they get their shares more cheaply than the public.

From the point of view of the promoter, the underwriter's commission makes serious inroads into his profits, although it largely removes the speculative nature of his enterprises.

All these parties—the promoter, broker, and underwriter—are interested in seeing that capital follows the most profitable channels. In the nature of things, promoters can succeed only by continuing to hold a good reputation. They are, for the most part, dependent upon the supply of capital from brokers and underwriters. As a rule, the underwriter deals with his own capital, although he may be reinforced by persons behind him. Brokers mostly raise capital by putting their proposition before clients who will lose no time in complaint if their money is wrongly invested. Hence, directly promoters are identified with unsuccessful concerns, no matter how honest they may be, they will experience great difficulty in getting brokers and underwriters to assist them.

**II. EMPLOYMENT FOR LABOUR.**—Quite a large number of persons take an interest in a business because they want to find some employment for themselves. There are others who regard the establishment of a business as an opportunity for finding employment for persons in whom they are interested, and for that purpose they are willing to risk capital. Further, an undertaking may be founded to provide employment for a particular class of persons ; e.g. the unemployed.



A person desirous of finding employment for himself may do so by the use of his own capital, although he may want to reinforce that with capital found elsewhere. Many business men of experience take the view, and probably there is a good deal of foundation for it, that it is not sound business to assist anybody with capital to start a business unless the founder has capital of his own to invest in it. As a rule, a man possessed of the qualities to establish a successful business is not likely to be the absolutely impecunious person. It is true there may be excellent reasons for his having no capital, but this is a matter for inquiry. It has to be borne in mind that the man who has no capital, and never has had any capital, cannot be expected to make the best use of it, since he has never had any experience in utilising it. Further, the administration of one's own capital is not the same thing as administering another person's capital.

Apart from the possession of any skill in the particular industry which he has undertaken, the founder of a business requires to be possessed of the following—

1. A considerable amount of energy.
2. Organising ability ; i.e. the ability to get other persons to do work on his lines.
3. Sufficient time to build up a connection before profits can be expected.

There is also the question as to whether the occupation to which he proposes to devote his energies is one for which there is any real demand in the sense that there is not a sufficient supply of labour in that particular calling. There are, of course, times when there is an opening for a new house in a particular direction, and times when the occupation is overcrowded.

### III. PROVISION OF A SUPPLY OF SOME PARTICULAR COMMODITY.

—The main object of establishing a business concern is to supply some kind of goods or services that might be required, which are not at present available, or are not available in a form which is regarded as entirely satisfactory. This motive gives rise to various forms of business activity which might be subdivided under five headings—

1. Individualistic Concerns.
2. Co-operative Undertakings.
3. Companies regulated by Parliament.



## 4. Government and Municipal Undertakings.

## 5. Trusts, Cartels, etc.

**I. Individualistic Concerns.** Under ordinary competitive conditions trade may be carried on, according to its business organisation, by any one of the following classes—

- |                          |                              |
|--------------------------|------------------------------|
| (a) The Sole Trader.     | (d) Public Limited Company.  |
| (b) Partnership.         | (e) Private Limited Company. |
| (c) Limited Partnership. |                              |

In accordance with the provisions of the Registration of Business Names Act, 1916, undertakings carried on in the United Kingdom under other than the true names of the owners must be registered with the Registrar of Business Names. In practice, the effect of this Act is to render it necessary to register the full Christian name and surname, and nationality if foreign, of every such sole trader or member of a partnership firm. In regard to Limited Companies, the same requirements as to registration and identity of the directors is required by the Companies Act, 1929. This is a protection to traders giving credit, who may reasonably desire to know the exact constitution of a concern with which they propose to deal.

A **SOLE TRADER** is a person who carries on business exclusively by and for himself. The leading feature of this kind of concern is that the individual assumes full responsibility for all the risks connected with the conduct of the business. He is not only the owner of the capital of the undertaking, but is usually the organiser and manager. The activities of such a concern are, as a rule, confined to a certain locality, and but seldom extend beyond the limits of a given country. This is usually due to—

- (1) Scarcity of capital ; (2) Limitation of managerial ability.

The chief types of concerns which take the form of organisation of the sole trader are retailers, hawkers, costermongers, and persons engaged in rendering direct services. In such concerns a simple form of organisation alone is required, and personal supervision can be exercised with success.

**PARTNERSHIP.** According to the Partnership Act of 1890, partnership is the relation which subsists between persons carrying on a business in common with a view to profit. The Act lays down rules for determining whether or not a partnership exists. The mere fact that a person receives a payment out of profits is not



# LEGAL CONSTITUTION OF INDIVIDUALISTIC CONCERNS

	Sole Trader.	Partnership.	Limited Partnership.	Public Limited Company.	Private Limited Company.
1	Consists of one person, viz., the owner of the business.	May consist of from 2 to 20 members (except in a banking partnership where they must not exceed 10).	Consists of one or more General Partners, and one or more Limited Partners. (The maximum number of members is 20, and in the case of a bank 10 members.)	Cannot consist of less than seven members.	May consist of 2 members, but not more than 50 (excluding employees and ex-employees).
2	The proprietor is personally liable for all the debts of the business.	Partners are liable for the full amount of the debts of the partnership.	The General Partners are liable without limitation for the debts of the firm. The liability of Limited Partners is limited to the amounts they contribute.	Each member's liability is limited to the nominal amount of capital undertaken to be contributed by him.	The members' liability is the same as in the Public Limited Company.
3	The proprietor may dis- pose of his business at any time.	Shares are not transfer- able.	A limited partner may transfer his share with the consent of the general partners.	Shares are freely transfer- able.	There is a restriction on the transfer of the shares.
4	Audit of the accounts is optional.	Audit of the accounts is optional.	Audit of the accounts is optional.	The audit of the accounts is compulsory.	The audit of the accounts is compulsory.
5	The Capital is introduced by the Proprietor, but he may obtain the use of outside loans.	The partners named in the articles of partnership introduce the capital.	The capital is introduced by the General and Limited Partners.	The public may be invited to subscribe the share capital.	The public must not be invited to subscribe the capital.
6	An annual balance sheet is not compulsory.	An annual balance sheet is not compulsory.	An annual balance sheet is not compulsory.	An annual balance sheet is compulsory, and a statement in the form of a balance sheet must be filed annually, at the Companies Registration Office.	An annual balance sheet is compulsory, but does not require to be filed at the Companies Registration Office.



by any means conclusive evidence of partnership. To constitute partnership, there must be evidence that the business is being carried on in the interest of the persons seeking to be held as partners. The fact that a retired partner or a widow of a deceased partner receives a share of the profits does not make them partners. It gives them neither the liabilities nor the rights of partners.

The chief characteristics of a *partnership* are—

- (1) Each partner is personally liable for the whole of the debts of the firm.
- (2) The capital is usually contributed by the partners themselves.
- (3) The profits or losses resulting from the conduct of the business are shared by the partners.

In an ordinary partnership, every partner is an agent of the partnership and is able to bind the firm in the ordinary course of the firm's business. If any serious alteration is proposed in the conduct of the business, it must be agreed to by all the partners. For example, if it is proposed to remove the partnership, or open a branch, they must all agree.

It is not uncommon for those who have their capital in the business and who have grown old, to take into partnership young men who have no capital. In this case, however, such partners do not always possess the right to veto any alteration in the conduct of the firm. One generally finds the rights of junior partners curtailed.

In professions, it is quite a common thing to have a partner who has no capital in the business and who has no interest in the goodwill. Sometimes he is remunerated by a share of profits, sometimes by a salary plus a share of profits, and often merely by a fixed salary. Such a partner is known as a *Salaried Partner*. The term suggests a partner with quite limited powers, whose position is not much more than that of a manager, but as regards the outside world he is looked upon as a partner, and is liable as such.

**LIMITED PARTNERSHIP.** The Limited Partnership Act of 1907 provides that a Limited Partnership must consist of one or more persons called *General Partners*, who shall be liable for all the debts and obligations of the firm, and one or more persons to be called *Limited Partners* who shall not be liable for the debts or obligations of the firm beyond the amount contributed.

This form of partnership is a development of the Continental idea, under which financiers, including bankers, may put capital



into a business and receive in return a rate of interest varying with profits without being liable as partners. A limited partner has no liability for the debts of the partnership beyond what he has put into the business. He is not allowed to take part in the management, but he can give advice. If things are going badly, however, and he tries to make the business better, he might be held to have taken part in the directing of the business as a partner.

**THE JOINT STOCK COMPANY.** A company in the widest sense of the term means an association of several persons who contribute money to a joint or common stock and employ it in some business, and share among themselves the profit or the loss arising from it. A company means an incorporated company. If a company is not incorporated, it is in reality a large partnership, even though it may be called a syndicate, and is governed by the law of partnership. But every association of more than ten persons for carrying on the business of banking, and every association of more than twenty persons for carrying on any other kind of business that has for its object the acquisition of gain, must be formed and registered as an incorporated company, because, if not so formed and registered, it will be an illegal association, with the result that—

(1) No action at law can be brought by it, against either a member or any other person ; and

(2) No person, whether a member or an outsider, can sue the association, because it cannot enter into any kind of contract.

An ordinary trading company is incorporated by registration under the Companies Act, 1929 ; and, in the great majority of cases, the liability of the members of the company is limited to the nominal amount of their shares. Every such company must have as the last word of its name the word "*Limited*," and the name of the company with the word "*Limited*" must be affixed to the outside of the place in which the business is carried on, and must also appear on all documents issued or used by the company. But where an association is about to be formed for the purpose of promoting commerce, art, science, religion, charity, or any other useful object, and the founders are willing to form it on the footing that its profits or income shall be applied exclusively in promoting the objects of the association, and that no dividend shall be paid to its members, the Board of Trade has the power to grant a licence authorising the registration of the



association with limited liability but without the addition of the word " Limited " to its name.

The essential difference between a company and a partnership is that a partnership is merely the aggregate of its individual members, whereas a company is a body corporate, or a corporation which, in point of law, is a person just as much as an individual, although its object is to limit his liability.

THE PRIVATE COMPANY. The Companies Act, 1929, provides for the formation of companies of two types limited by shares, namely, public and private companies. The Act, in Section 26, lays down the conditions which must be complied with if a company is to enjoy the privileges of a private company. These are—

(1) *Restricts Transfer of Shares.* A private company must, in its Articles of Association, restrict the rights of its members to transfer their shares. This does not mean that transfer is prohibited, but that the inherent right of transfer which shareholders usually possess must be modified so that no open market dealing takes place. As a general rule the articles restrict transfer to specified relatives of the member or to other members, giving the latter an option of purchasing before any transfer is made to outsiders.

(2) *Limits Membership to Fifty.* A private company may consist of a minimum of two members and a maximum of fifty, whereas a public company has a minimum of seven and no upper limit. This provision is relaxed by making an exception in the case of past or present employees of a private company who have become shareholders whilst in the service of the company. This exception was inserted to encourage the introduction of profit-sharing and co-partnership schemes which might have been beyond the power of a private company if such employee shareholders had been included in the maximum membership of fifty.

(3) *Prohibits Invitation of Public Subscription.* A private company is prohibited from appealing to the public for subscriptions to an issue of shares or debentures, whereas in the case of a public company this is, of course, the customary method. Hence the private company must raise its capital requirements from a restricted circle of investors and, in the event of additional capital becoming necessary to finance new developments, cannot resort to an appeal to the public without losing its status as a private company.

We may regard the private company as a kind of transitional



form of legal constitution between the public company and the partnership. It confers the privilege of limited liability upon its members and yet is subject to a minimum of restriction by the law. For example, although an annual return of members must be made to the Registrar of Companies, no balance sheet need be sent with it by a private company, whereas a public company must submit a balance sheet containing a certain amount of information prescribed by statute. Again, a public company must have a minimum of two directors, whereas in the case of a private company this requirement does not apply. The private company, therefore, provided it complies with the statutory requirements, can conduct its business on very similar lines to a partnership, except that the members of such a company enjoy the important advantage of limited liability. Finally, private companies afford facilities to the testator whose capital is sunk in his own business to divide his estate among his relatives without disturbing the financial arrangements of the undertaking, and at the same time limiting the liability of those to whom the business is left.

Frequently the shareholders consist only of the members of one family, yet if one person holds nearly all the shares, the company is still regarded as a distinct entity. In this case it is spoken of as a *one-man* company.

**II. Co-operation.** Those who want some particular kind of commodity may combine together and themselves establish a business, so that they may be regarded as the proprietors and also the customers of that business. There are many examples of such co-operation, although the precise organisation varies somewhat under different circumstances.

In connection with the business of insurance, there is a whole group of concerns which might be brought under this heading. The most obvious form is what are called mutual offices, which sometimes deal exclusively in life assurance and sometimes in life assurance combined with other kinds of insurance. The distinctive feature of such concerns is that the policy holders are the sole proprietors, and whatever profits there are may be applied in strengthening the financial position, in reducing future premiums, or in making a return at the end of the year of a portion of the past year's premiums.

Again, in many seaport towns a similar organisation is established among shipowners with regard to their ships. Insurances



which either cannot be underwritten at Lloyd's, for one reason or another, or are thought to be too small to be worth taking to Lloyd's, are often provided for by insurance clubs, the members of which are all carrying on business at the same port and are all known to each other. They work on the same lines as a mutual insurance company, although the business represents a more rudimentary form of insurance. For instance, if there are a dozen ship-owners in a certain seaport, each of whom owns, on the average, three or four ships, they will place their business on a less speculative basis if they mutually agree among themselves to bear a due proportion of each other's losses. The position will then be that each shipowner will have to pay something, but in no year will any of them have to pay so large a sum as to become seriously embarrassed. So long as it can be arranged on these lines and limited to comparatively small amounts, the result may be to spread over a score or more persons a risk which would otherwise have to be borne by one individual.

Another form of co-operation in kind, although not in name, has arisen in connection with what are called "building societies." *Building societies* are rather peculiar institutions, in that they are organised on different lines from other business concerns. The function of a building society is really twofold—

(1) To receive deposits from those of its members who may care to invest money with it at interest ; and

(2) To lend out, from time to time on the security of mortgage of leasehold or freehold property, such money as it may have.

Hence, the business of a building society resembles that of a bank or money-lending society. The distinctive feature of a building society is that it locks up its assets, whereas it raises the money which it lends in this way from other parties, who, when it suits them, can ask for the return of their money. Building societies thrive best in colliery districts, where there is a common interest to bind the members, and hence they are not so easily liable to scares.

What is ordinarily meant by a *co-operative society* is a society registered in this country under the Industrial and Provident Societies Act, 1893. Under that Act societies may be formed which for all practical purposes are limited companies with a difference. Like limited companies, they may carry on any desired kind of business. On the other hand, like building societies, they



raise their capital either by accepting loans repayable at short notice or by issuing so-called shares, which are paid up by weekly or monthly instalments. These industrial and co-operative societies mostly run a general stores, and for the most part buy what they sell from a central society formed on similar lines, which is called the Co-operative Wholesale Society. The idea is that the consumers, by combining, shall be able to eliminate the profits of the middleman and capitalist, and obtain for themselves all the profits connected with the supplying of the goods which they require for their own use. At the end of the year, when profits are ascertained, dividends are paid *pro rata*, according to the purchases of the various members during the year, the capital receiving only a fixed rate of interest, which is agreed upon beforehand.

**III. Companies Regulated by Special Act of Parliament.** The Government sometimes grants what may be called concessions to companies to do certain kinds of work or pursue certain kinds of activities, either in this country or elsewhere. These concessions are usually more or less in the nature of monopolies. Under this class are to be grouped such diverse undertakings as railways, tramways, canals, waterworks, or gas and electric light works, and such concerns as the British South Africa Company or the old East India Company, which, for all practical purposes, had powers almost analogous to those of Sovereign States. In each case the idea here is clearly that some special concession must be granted by the State to encourage capitalists to combine to provide the necessary capital to carry through the scheme.

The chief peculiarity of these concerns is that the State constructs them so that it can exercise some kind of supervision over them, and that can be effected in one of three ways—

(1) The limitation of the amount of capital that can be raised to some prescribed sum which is sufficient to make a start, but insufficient to continue with, so that every time it requires more capital, it is obliged to apply to Parliament for increased powers, and all who have a grievance against the company are entitled to be heard prior to such powers being granted.

(2) There are usually provisions as to the charges which these companies are entitled to make for their services. The charges are either prescribed beforehand or some scheme is established which will enable them to be fixed from time to time according to



circumstances. They are fixed in various ways according to the requirements of the position, but the company cannot charge just what it likes ; nor can it make a charge merely because it is necessary to enable the company to carry on the business at a profit. For example, water is supplied at a certain rate, and whether it is used or not the charge is made. With regard to gas, the price to be charged for the gas depends upon the quantity used, and is fixed at a standard rate, and the provision is that the standard rate must not be exceeded, but may be reduced, and, if it is reduced *pro rata*, the dividend paid by the company to its proprietors may be increased. Assuming that the price of gas is fixed on a reasonable basis to allow a fair return by way of dividend to the proprietors, then if, as a result of efficient manufacture, the company is able to manufacture gas more cheaply, the advantage is shared between the proprietors and consumers.

(3) The State reserves for itself or the local authority the right to purchase the undertaking at the end of a certain number of years, so that, instead of the concession being freehold, it is merely leasehold. This is the case with regard to many electricity, gas, water, and other companies.

**IV. Government and Municipal Undertakings.** Sometimes the Central or Local Government may embark upon business enterprise, either in competition with existing undertakings or to fill vacancies where there are no concessionaire companies. There are many examples of such enterprises. In the case of the Central Government, there is the Post Office Savings Bank, National Insurance, the delivery of parcels and of letters through the Post Office, etc. In the case of local authorities, there are many different forms of activity, such as waterworks, gasworks, tramways, electric light, etc.

The primary reason for the establishment of such undertakings is due to one or other of the following—

(1) To make profits out of the carrying on of these businesses which would prove a source of income to the authority, and thus enable it to manage with lower rates or taxes than would otherwise be necessary ; or

(2) To provide a service giving better value for money than any purely business concern could be expected to give.

A public authority can raise capital more cheaply than an ordinary business concern, because the loans which it raises are



secured by the rating authority of the Corporation borrowing the money.

If Government trading is to be conducted to proper business advantage, it must be a monopoly. That is to say, the service rendered is usually one in which there is not sufficient scope to throw it open to competition, because there would not be enough business for two or more concerns to make a livelihood out of it. Hence, it may be argued that the monopoly should be under the control of a public body, to guard against abuse.

**V. Trusts and Cartels.** Sometimes a number of persons or business houses will form a temporary combination to achieve some particular purpose in connection with a specified trade or profession. If a combine is formed, and it is agreed that a particular article shall not be sold for less than a certain price, then a monopoly is set up. A combination can work a monopoly so long as it is strictly a monopoly, but it very often breaks down for some reason or another. The most highly developed form of combination is known as a trust, and originated in America. The cause of the development of trusts is to be found in the concentration of production which arises when competition acts upon improved processes and leads to the invention of better processes. For undertakings of that kind, large capitals are required, so that only large businesses could take them up, and where inventions or discoveries, such as petroleum, etc., have been made, the large scale enterprises have tended to absorb the smaller ones.

A trust is really a partnership of companies and is usually incorporated as a *holding company*. Each company involved remains a legal entity, but the control definitely passes to the holding company and the actual business policy of the subsidiary companies will inevitably be changed, having regard to the interests of the combine as a whole. Thus the shareholders of a number of separate companies agree to combine into a trust, and thus surrender their shares to one central board of trustees. This board receives an irrevocable power of attorney to act for the shareholders, who receive in return the trust certificates which represent their share in the undertaking, and the profits are divided among the shareholders according to the number of certificates held.

Where competitors are powerful but few in number, they often



come to some understanding among themselves with regard to the sale of their goods. This agreement may have reference to terms of payment, or regulation of output, but so long as the parties to the agreement retain their separate existence as single businesses, the combination is some form of cartel, and differs from the trust in being a looser form of combination.

### TEST PAPER XIV

1. What are the chief motives which lead to the establishment of business concerns?

2. In what way do the profits of a business determine the flow of Capital?

3. What are the chief factors which influence investment of Capital in industry?

4. Name the classes of persons who are engaged in directing the flow of Capital into different industries.

5. Explain the duties of a company promoter.

6. Show how brokers assist in the establishment of business concerns.

7. What are the duties performed by an underwriter in the formation of a company?

8. Enumerate any points which should be noticed when providing employment for others.

9. Mention any instances of undertakings which have been started with the object of providing employment for labour.

10. Compare, in tabular form, the relative advantages and disadvantages of Partnerships, Private Companies and Public Companies as forms of business organisation.

11. Distinguish between concerns which are worked on a co-operative basis and those which are essentially individualistic.

12. Mention some of the chief types of co-operation.

13. Say what you know of Mutual Insurance Societies, Building Societies, and Industrial and Provident Societies.

14. Some companies are regulated by Parliament. Account for this, and give illustrations of such companies.

15. Compare the management of a business regulated by Parliament with one which is owned and controlled by a Municipality.

16. Enumerate the chief forms of enterprise which are conducted by Government undertakings.

17. Compare Government undertakings with those which are privately owned and controlled.

18. To what extent is the company promoter dependent upon the services of the broker and the underwriter in the establishment of a business concern?

19. What are the advantages and disadvantages of a partnership?

20. What relative advantages accrue to the carrying on of a business by (a) an individual, (b) a firm, (c) a private limited company? What classes of businesses are best suited to each of these three categories and why?

21. Who precisely obtains the profit or suffers the loss arising from industrial enterprise in—

(a) A private business.

(b) A public joint stock company.

(c) A co-operative retail society.

(d) A municipal undertaking.

Do you consider this question important in considering the probable efficiency of the enterprise?



## CHAPTER XV

### THE JOINT STOCK COMPANY

**JOINT STOCK COMPANIES AND COMMERCIAL DEVELOPMENT.**—The general trend of modern business enterprise is in the direction of an increase in the size of the typical unit engaged in most industries and trades. This tendency may be ascribed to two sets of causes, namely, technical progress and economic factors. In the first place, most manufacturing and constructional industries have, during the last one hundred years, seen the introduction of mechanical inventions, with the result that hand labour has been progressively displaced in favour of the machine. The new machinery has usually had the dual effect of stimulating output and reducing costs of production, so that in the majority of cases lower selling prices have stimulated sales and have led to a progressive expansion in the scale of the enterprise. Yet even in those industries where mechanisation has not been so apparent, other factors have been at work to increase the size of the business undertaking. Attempts have been made at expansion in order to reap the benefit of certain economies which attend the conduct of business operations on a large scale—economies of buying or of selling, as in the case of retail trading organisations, or of specialisation of ability.

The result of this expansion, whether arising from technical or from economic motives, has been to increase enormously the capital requirement of the average industrial or commercial undertaking. There will be an increased outlay of fixed capital on factory buildings, plant, and machinery in the case of the manufacturing concern, and on business premises, fixtures and fittings, and the like in the case of the trading business. Again, the need for circulating capital will increase to a corresponding extent; stocks of raw materials and finished goods must be held, the wages and salaries of a large staff must be paid, more or less extended credits must be granted to customers, and heavy establishment charges must be met. Altogether, a very considerable capital investment of a permanent nature is called for and the problem of securing this investment arises.

The solution of the problem has been found in the evolution of



the modern joint stock company which has been judicially defined as "an association of many persons who contribute money or money's worth to a common stock and employ it in some trade or business, and who share the profit and loss (as the case may be) arising therefrom." The earliest associations of persons for trading purposes were of the *regulated* type, i.e. companies in which every member traded solely on his own behalf, subject only to certain regulations and restrictions imposed by each company. By the end of the seventeenth century, however, a form of organisation similar to that of the modern joint stock company had emerged, although it had, as yet, obtained no legal recognition, except by means of charters or special Acts. Many of these early joint stock companies obtained exclusive privileges for trading or for manufacture in return for a cash payment, a fact which led one writer to characterise them as "simply one of many shifty devices for raising money independent of parliamentary supplies." Much of the prejudice against the joint stock company which existed during the seventeenth century was due to this monopolistic feature, which was frequently abused.

The early eighteenth century saw a wave of financial speculation, the outstanding example being connected with the South Sea Company, though the public lost large sums of money in projects much more uncertain and fantastic than this. The failure of this speculative boom produced widespread ruin and effected a vast redistribution of wealth, and led to the passing of the "Bubble Act" of 1720, by which persons concerned in joint stock speculations, with the exception of two specified companies, were subjected to heavy penalties. This Act was not repealed until 1825, and although during the greater part of its currency it was practically a dead letter, it none the less acted as a deterrent to joint stock enterprise. The next important advance was made under the Companies Act of 1855, which adopted the modern principle of limited liability, whereby the liability of any shareholder for the debts of the company was limited to the unpaid portion of the share capital held by him. The original Act has been amended and amplified on a number of occasions in the light of experience, the latest enactment being the Companies Act of 1929, which now governs all registered companies in this country.

**ADVANTAGES OF THE JOINT STOCK COMPANY.**—If it had not



been for the development of companies with limited liability under the regulative provisions of the Companies Act, there would have been great difficulty in meeting the growing financial needs of modern enterprise, and without this assistance many of the great mechanical inventions by which the technique of industry has been transformed might have remained undeveloped. The importance of this form of enterprise may be gauged from the fact that there are more than 100,000 companies registered under the provisions of the Companies Acts. The popularity of this type of legal constitution may be ascribed to the existence of a number of important advantages, the chief of which will now be examined—

(1) **Continuity of Existence.** Upon the registration of a joint stock company under the provisions of the Companies Act, 1929, there is brought into existence a new legal entity entirely separate and distinct from the persons of the promoters by whose efforts it is created. It may own and dispose of property, enter into binding contracts, and incur fines and penalties for the acts of its servants. The independent legal status of the joint stock company was confirmed in the famous leading case in company law of *Salomon v. Salomon & Co.* (1897). Here it was held that even in the case of a so-called “one-man” company, i.e. where one person holds practically all the shares and the other shareholders have only one share each, the company is a separate entity in law from the principal shareholder. Neither does the relationship of principal and agent exist between the company and its shareholders making the latter liable to indemnify the company against the debts which it incurs. This separation of identity confers upon the company what Blackstone called a kind of legal immortality. In other words, although individual shareholders may die, the company still continues in existence, always provided, of course, that the number of members does not fall below the legal minimum (see page 143). It could be pointed out, however, that although the joint stock company possesses the *potentiality* for perpetual existence, it by no means follows that this is realised. Such facts as are available show that the mortality rate is very high indeed. A recent investigation into the history of some 5,000 companies registered between 1856 and 1865 showed that about 36 per cent ceased to exist within five years of promotion, whilst only 8 per cent have survived to the present day in their original form.



In respect of its continuity of existence, the joint stock company differs essentially from the partnership. The Partnership Act, 1890, stipulates a number of circumstances in which a dissolution of partnership may take place, such as the death or bankruptcy of a partner, or in the absence of an agreed time for the continuance of the firm, upon notice of withdrawal being given by any partner. This arises from the fact that, in the case of a partnership firm, the law does not recognise the existence of the firm as a separate entity, but merely acknowledges the partners in their personal capacity. Hence, in addition to the ordinary risks of business, which all organisations alike must face, the partnership is much more vulnerable than the joint stock company to dissolution from within, and may be regarded as a much less stable form of enterprise.

(2) **Limitation of Liability.** The liability of the shareholders of a registered company is limited to the amount of the nominal value of the shares which they have acquired. Thus, if a person has purchased 100 shares of £1 each from a company and has paid 10s. per share, or £50 in all, he can be compelled to pay no more than the outstanding balance, i.e. £50, and upon payment his responsibility ceases. This limitation of liability again arises from the fact which we have already mentioned—the separate legal identity of the company. The company enters into contracts and deals with property in its own name so that its creditors have to look to the company for payment and not to the individual directors or shareholders. If the property of the company is insufficient to meet its commitments, the creditors have no right of action against the shareholders, that is, assuming no legal irregularity. Here again we have an important point of difference between the company and the partnership. The creditors of the partnership have a right of action against all or any of the partners, and may enforce the judgment not only against the partnership property, but also against the private possessions of the individual partners.

This limitation of liability of the members of a joint stock company has an important result in the stimulation of investments. Many people will be naturally reluctant to invest money in an enterprise which may involve them in unlimited liability in the event of adverse business conditions. This is particularly true of the small investor who will probably hoard his savings rather than expose himself to such a risk. Now the hoarding of savings in the



place of investment is wasteful both to the individual and to the community. The individual fails to obtain any tangible return as a reward for his thrift, so that he is always exposed to the temptation of spending for immediate consumption instead of saving at all. From the standpoint of the community as a whole there is a diminution of national wealth due to a non-productive use of savings. With the introduction of the principle of limited liability this reluctance to invest was speedily overcome, for now the individual knew precisely the extent of his commitments.

(3) **Transferability of Shares.** A further device by the aid of which the joint stock company has stimulated investment is the transferable share certificate. As we have already pointed out, modern business enterprise requires the investment of large sums of capital in fixed and in circulating assets. Capital so invested, particularly in fixed assets, is difficult to realise except at a heavy loss and any attempt to do so must paralyse the activities of the business, or, at best, seriously impair their efficiency. Hence when once capital has been invested in a business, the investor must be prepared to leave it there unless he can find some one who is willing to buy his interest in the undertaking, in which case no disturbance takes place so far as the business itself is concerned. This problem of finding a buyer for an interest in a business undertaking is simplified by the device of the transferable *share certificate*. A person, on subscribing to the capital of a joint stock company does so by purchasing a number of shares of equal nominal value, the usual denomination being one pound. Subject to any restrictions imposed by the company, a shareholder possesses complete freedom to dispose of all or any of the shares which he has purchased, so that should he wish to realise his investment, he has only to find a buyer who will offer a satisfactory price and the transfer can take place upon the performance of the requisite legal formalities. This task of transfer would, even then, present considerable difficulty were it not for the fact that the way is made smoother by the existence of a market for dealing in such securities, namely, the Stock Exchange. Through the medium of this institution a price is fixed for a wide range of security on the basis of the expert judgment of dealers, and the services of this market are available to the investor.

The transferable share saves the joint stock company from yet another of the difficulties associated with the partnership business.



The right to restrict the transfer of shares, where it exists, is vested in the directors and in any case must be used with care, so that a member of a company can sell his shares without reference to the other shareholders. In the case of a partnership, however, a new partner cannot be introduced without the consent of all the other partners. The reason for this difference in the law is not far to seek. Membership of a company does not, of itself, confer any right to interfere in the management, but in the case of a partnership, in the absence of special agreement, all partners have a right to share in the management of the business. It is only simple justice, therefore, that partners should be protected from the danger of having an unwanted co-partner thrust upon them. None-the-less, this circumstance raises difficulties if one member wishes to withdraw, and the remaining partners may be put to considerable embarrassment in buying out the retiring partner if they wish to continue the business.

(4) **Accumulation of Large Resources.** The foregoing considerations, particularly the limitation of liability and the possibility of transferring the ownership of shares, have served to stimulate the process of capital investment, particularly from the small investor. It has recently been shown by Mr. Hargreaves Parkinson<sup>1</sup> that in the case of the ordinary shares of an average British company with a large capital and an active market for its shares, approximately 40 per cent of the shareholders hold fewer than 100 shares each, whilst nearly 90 per cent hold fewer than 500 shares each. We are justified in concluding therefore that it is the small investor who provides the bulk of the finance by which "big business" is carried on at the present day. The large capital accumulations which are essential to the large businesses of the present day could never have been provided on the basis of a partnership arrangement. A limited number of men could never possess between them the capital resources necessary. By providing a means whereby a widespread appeal can be made to investors of all classes, the joint stock company overcomes the difficulty. Thus Imperial Chemical Industries, Ltd., has drawn its capital of over £43,000,000 from some 124,000 shareholders.

(5) **Best Use of Economic Resources.** In theory, at all events, the joint stock company offers a possibility of turning the economic resources of a community to the best possible use. In a developed

<sup>1</sup> *Scientific Investment.*



# THE LEGAL FOUNDATION OF A JOINT STOCK COMPANY

## EXTERNAL RELATIONSHIPS governed by MEMORANDUM OF ASSOCIATION

### FORM

Printed, written or typewritten.  
Stamped with 10s. deed stamp.  
Bearing Companies' Registration Fee Stamps.  
Signed by Subscribers.

### CONTENTS

- (1) Name Clause.
- (2) Domicile.
- (3) Objects Clause.
- (4) Limitation of Liability.
- (5) Capital Clause.
- (6) Association Clause.

## INTERNAL RELATIONSHIPS governed by ARTICLES OF ASSOCIATION

### FORM

- (1) Printed.
- (2) Divided into numbered paragraphs.
- (3) Stamped with 10s. deed stamp.
- (4) Signed by each Subscriber to the Memorandum.

### CONTENTS

- | Shareholders   | Directors   | Public  |
|--|---|---|
| <ol style="list-style-type: none"> <li>(1) Rights of different Classes.</li> <li>(2) Meetings.</li> <li>(3) Voting Powers.</li> <li>(4) Calls on Shares.</li> <li>(5) Powers of Forfeiture.</li> <li>(6) Company's right of Lien.</li> </ol> | <ol style="list-style-type: none"> <li>(1) Number and Remuneration.</li> <li>(2) Meetings.</li> <li>(3) Powers and Duties.</li> <li>(4) Qualification.</li> <li>(5) Provisions for Vacation of Office.</li> </ol> | <ol style="list-style-type: none"> <li>(1) Borrowing Powers.</li> <li>(2) Accounts.</li> <li>(3) Transfer of Shares.</li> </ol> |



community we shall find a large amount of capital in the form of small savings seeking profitable investment, whilst at the same time there will be a limited number of men with exceptional business ability who can be trusted to make a success of a business enterprise. By the formation of a joint stock company an outlet for investment is provided, whilst the company, by employing the best talent available, is enabled to make the transaction a profitable one for its shareholders. Through the joint stock company, capital and business ability may be linked together for the benefit both of the individual investor and the whole community.

It needs little emphasis, however, that although such a possibility exists, it frequently fails to be realised in actual practice. All kinds of difficulties and complications arise when the ownership of capital is separated from the active control and management of the enterprise in which it is invested. Moreover, we have to bear in mind that the system is productive of many ill-conceived projects, not necessarily always fraudulent, which cause the investor heavy annual losses of capital.

**REGISTRATION OF A COMPANY.**—A joint stock company of the type which we are here considering will be formed for the purpose of carrying on some type of industrial or commercial activity by a group of persons known as the promoters. Although the work of the promoter is essential to the formation of the modern company, no statutory definition has been laid down, although a promoter has been judicially defined as “one who undertakes to form a company with reference to a given project and to set it going, and who takes the necessary steps to accomplish that purpose.” It is the promoters who conceive the project which is to form the business of the company and who enter into any preliminary negotiations which may be necessary. Thus, if property is to be taken over, they will arrange the terms of sale or possibly actually acquire the property on behalf of the company which is to be formed. It has been clearly established as the result of a large number of legal decisions that the promoters of a company stand in a special position of trust to the company which they are forming, and the principles of the law of agency and of trusteeship have been extended to this relationship. The promoters must make complete disclosure of their interest in the transaction, and must on no account make a secret profit at the expense of the company.



Before a company can come into existence as a legal entity it must be registered with the Registrar of Companies at Bush House. Hence when the preliminary matters have been settled and the way is clear for the flotation of the company, the promoters will proceed with the formalities of registration. These consist in the preparation and lodging of a number of documents with the Registrar and also the payment of certain stamp duties and fees. This process of registration is necessary for the protection of the investing public who may be asked to subscribe to the capital of the company and also for the protection of all other persons who may, sooner or later, enter into business relations with the new company. The documents which are lodged on registration give what is considered to be an essential minimum of information regarding the constitution and management of the company. When the documents have been registered at Bush House any member of the public, upon payment of a nominal fee, may inspect them, so that there is a presumption at law that every person dealing with the company is aware of their contents.

The following documents have to be filed upon registration—

(1) **Memorandum of Association.** This is the most important document connected with the company since it defines the constitution of the undertaking in its relation to the outside world. As will be seen from an examination of the abridged specimen on page 162, the Memorandum consists of six main clauses, namely—

(a) **THE NAME CLAUSE**, which states the name of the company in full, the Companies Act providing that the name must end with the word “Limited” unless permission be obtained from the Board of Trade to omit this. A company may select any name it pleases, except that it may not register a name identical with that of a company already in existence, or so closely resembling it as to be calculated to deceive the public. This measure is designed to protect the goodwill of existing companies. In addition, the Companies Act prohibits the use of a number of words including Royal, Imperial, Municipal, Chartered, and Co-operative without the consent of the Board of Trade.

(b) **SITUATION OF REGISTERED OFFICE.** The second clause states what is known as the *domicile* of the company, i.e. the country in which the registered office is to be situated. For the purpose of



# SPECIMEN MEMORANDUM OF ASSOCIATION

The Companies Act, 1929

Company Limited by Shares

## MEMORANDUM OF ASSOCIATION of

### THE ENTERPRISE ENGINEERING COMPANY, LIMITED

1. The name of the Company is "THE ENTERPRISE ENGINEERING COMPANY LIMITED."
2. The registered office of the Company will be situate in England.
3. The objects for which the Company is established are—
  - (a) To conduct, enter into and carry on in a wholesale or retail capacity the business of manufacturers of and dealers in and merchants and factors of Radiators, Boilers, and all kinds of Heating Apparatus, China, Porcelain or Pottery Articles, and all accessories and goods used or dealt with in connection therewith.
  - (b) To carry on business as ironmongers, turners, brassfounders, engineers, founders, smiths, machinists, tool-makers, metal workers, furnace designers and constructors, boilermakers, millwrights, iron and steel converters, metallurgists and electrical engineers, carpenters, joiners, wood-workers and cabinet makers, and to deal in (either wholesale or retail) all articles and things which are capable of being manufactured in such businesses.
  - (c) To acquire, undertake and carry on the whole or any part of the business, property and liabilities of any company carrying on any business which the Company is authorised to carry on or possess, or which may seem to the Company capable of being conveniently carried on or calculated directly or indirectly to enhance the value of or render profitable any of the Company's property or rights or any property suitable for the purposes of the Company.
  - (d) To enter into partnership or into any arrangement for sharing profits, union of interests, co-operation, joint adventure, reciprocal concession, or otherwise, with any company or person, or with any employees of the Company, including in such case if thought fit the conferring of a participation in the management or its directorate or with any company carrying on or engaged in any business or transaction capable of being conducted so directly or indirectly to benefit the Company, and to give to any company or person special rights or privileges in connection with or control over this Company, and in particular the right to nominate one or more directors of this Company. And to lend money to, guarantee the contracts of, or otherwise assist any such company, and to take or otherwise acquire shares or other securities of any such company, and to sell, hold, re-issue, with or without guarantee, or otherwise deal with the same.
  - (e) To borrow or raise and receive the payment of money in such manner as the Company shall think fit and in particular by the issue of debentures or debenture stock, perpetual or otherwise charged upon all or any of the Company's property, including its uncalled capital, and to purchase, redeem or pay off any such securities.
  - (f) To draw, make, accept, endorse, discount, execute, and issue promissory notes, bills of exchange, bills of lading, warrants, debentures, and other negotiable and transferable instruments.
  - (g) To sell or dispose of the undertaking of the Company or any part thereof, for such consideration as the Company may think fit, and in particular for shares whether fully or partly paid up, debentures or securities of any other company, whether or not having objects altogether, or in part, similar to those of the Company, and to hold and retain any shares, debentures and securities so acquired.
  - (h) To do all such things as are incidental or conducive to the attainment of any of the above-mentioned objects.
4. The liability of the members is limited.
5. The capital of the Company is £1,000,000, divided into 1,000,000 shares of £1 each.

We, the several persons whose names and addresses are subscribed, are desirous of being formed into a Company in pursuance of this Memorandum of Association, and we respectively agree to take the number of shares in the capital of the Company set opposite to our respective names.

Names, Addresses, and Descriptions of Subscribers	Number of Shares Taken by each Subscriber
George Robinson, 10 Snow Hill, Newport, Engineer	One
Albert Brown, 109 Ninian Road, Cardiff, Independent	One
Frank Hall, 45 Wind Street, Swansea, Accountant	One
Robert Johnston, "Sunnyside," Rhiwbina, Cardiff, Engineer	One
Alfred Williams, 98 Queen Street, Cardiff, Solicitor	One
John J. Jones, 14 The Parade, Penarth, Clerk	One
James Jackson, 6 Dywrig Street, Cardiff, Independent	One

Dated this 1st January, 194—

Witness to all the above signatures,

William A. Harrison,  
Principality Buildings,  
Cardiff, Solicitor.



company registration Wales is deemed to be part of England. Once the domicile has been selected it cannot be changed, but the company can move its registered office about within the country of registration. Thus, if a company is domiciled in England it could move its registered office from London to Cardiff or to Liverpool, but could not move to Edinburgh.

(c) OBJECTS CLAUSE. This clause is fundamental to the whole existence of the company, for it states what the company may do and effectively defines its relationship with the outside world. Once a company has been registered with certain objects it cannot depart from them or change them in any way except with the permission of the Court—permission which cannot readily be obtained. Any Acts purporting to be done by the company but falling outside the objects clause are said to be *ultra vires* or “beyond the powers” of the company and, as such, are not binding upon it. They may, of course, be enforceable against the directors or officers of the company in certain cases, but they cannot be ratified by the company, even though every member is in agreement with them. If the company ceases to carry on its main object for any cause whatsoever, then it must be wound up.

(d) LIABILITY CLAUSE. This is a simple statement to the effect that the liability of the members is limited. This limitation of liability may be either by shares or guarantee, but the usual presumption is that liability is limited by shares. In such circumstances the total possible liability to which any shareholder may be subjected is limited to the nominal value of his shares and, when these are fully paid up, his responsibility ceases.

(e) CAPITAL CLAUSE. This clause must state the amount of the capital with which the company proposes to be registered and the mode of its division into shares of fixed amount. The Companies Act imposes no regulation as to the absolute amount of capital of a company nor regarding the nominal value of the shares into which it is divided. The usual denomination of the shares of a company is £1, since this is a convenient amount for most classes of investors. The Companies Capital Duty of 10s. per cent is payable upon the capital as stated in this clause. The amount of the registered capital may be altered with the sanction of the Court, though a reduction of capital will be permitted only after a most careful inquiry into the circumstances which have occasioned it.



(f) **ASSOCIATION CLAUSE.** This is the final clause of the Memorandum and takes the form of a declaration by the signatories that they are desirous of being formed into a company and that they are prepared to take up and pay for the number of shares set opposite their respective names. The Memorandum must bear the signatures of at least seven persons in the case of a public company and at least two in the case of a private company, whilst each must agree to take up not less than one share in the capital of the company. The Memorandum must bear a 10s. deed stamp and also an impressed fee stamp varying in amount from a minimum of £2 to a maximum of £50 in accordance with the amount of the nominal capital.

(2) **Articles of Association.** This document contains the regulations which govern the internal management of the company as distinct from the Memorandum which controls its external relationships. The Articles must be signed by the signatories to the Memorandum and must bear a 10s. deed stamp as well as a registration fee stamp of 5s. In the case of a public company, it is not essential that special Articles of Association should be drawn up, and if no Articles are registered the company is considered to have adopted a set of model articles known as Table A, which are contained in the First Schedule of the Companies Acts. This course is not open to a private company, however, since this type of undertaking must limit the number of its members to fifty, and restrict the right to transfer shares—matters which are inconsistent with certain clauses of Table A.

Alteration of the Memorandum of Association when once it has been registered is, as we have seen, a matter of some difficulty, and can take place only with the consent of the Court. Alteration of the Articles of Association, however, is a matter which rests purely with the shareholders of the company since the Articles are concerned merely with its domestic affairs. This power of alteration is limited by certain necessary restrictions. The company cannot alter its Articles in such a way as to contravene the powers conferred upon it by its Memorandum; neither can it do anything which is illegal under the Companies Act. Finally, this power of alteration must be exercised in good faith and for the benefit of the company as a whole. In other words, if the alteration is so extravagant that no reasonable man could consider it for the benefit of the company, or



so oppressive as to cast suspicion upon the honesty of those who passed the resolution, the alteration will be invalid.

(3) **Statement of Nominal Capital.** In addition to the capital clause contained in the Memorandum of Association, a statement of nominal capital must also be registered showing the amount of the registered capital, that is, the same amount as shown in the Memorandum. It is upon this document that the Companies Capital Duty is actually paid.

(4) **Statutory Declaration.** This is a declaration to the effect that all the requirements of the Companies Act, 1929, have been duly complied with, and is made either by a solicitor engaged in the formation of the company, or by a person named in the Articles as a secretary or director. There is a registration fee of 5s.

(5) **List of Persons Who Have Consented to Become Directors.** The company must, at the time of registering the Memorandum and Articles, lodge a list of persons who have consented to become directors. This does not apply in the case of a company which has no share capital or which is being converted from a private to a public company. It should be noted that all public companies which are registered under the Companies Act, 1929, must have at least two directors.

(6) **Consent to Act.** It is frequently the practice to name the first directors of a company in the Articles of Association, but no person named in this way is validly appointed until he has delivered a written consent to act to the Registrar. In the same way he may not be named in the Prospectus or Statement in Lieu of Prospectus as a director without complying with the same formality. Furthermore, each director must have either—

- (a) Signed the Memorandum for his qualification shares; or
- (b) Taken his qualification shares from the company and paid or agreed to pay for them; or
- (c) Signed and delivered to the Registrar an undertaking to take up and pay for his qualification shares; or
- (d) Delivered to the Registrar a statutory declaration to the effect that a number of shares, not less than his qualification, are registered in his name.

(7) **Notice of Situation of Registered Office.** As we have already seen, the Memorandum contains a statement as to the domicile of the company, but makes no statement as to the exact location of the



# **STAGES IN THE FORMATION OF A PUBLIC LIMITED COMPANY UNDER THE COMPANIES ACT, 1928**

STAGE	LEGAL FORMALITIES	COMMENTS
I. Preliminary Work of Promotion.	<ol style="list-style-type: none"> <li>(1) Draft Memorandum of Association.</li> <li>(2) Draft Articles of Association.</li> <li>(3) Prepare Preliminary Contracts.</li> <li>(4) Prepare Draft Underwriting Agreements.</li> <li>(5) Draft Prospectus.</li> </ol>	At this stage, the Company, as a legal entity, has no existence, and the Promoters must undertake everything on their own responsibility. They will endeavour to enlist the necessary financial support against the time when the Company is floated.
II. Incorporation.	<ol style="list-style-type: none"> <li>(1) Registration of— <ol style="list-style-type: none"> <li>(a) Memorandum of Association.</li> <li>(b) Articles of Association.</li> <li>(c) Statement of Nominal Capital.</li> <li>(d) List of Persons who have consented to become Directors.</li> <li>(e) Written Consent to Act as Director.</li> <li>(f) Declaration of Compliance with Requirements of the Act.</li> </ol> </li> <li>(2) Notice of Situation of Registered Office (within 28 days of incorporation).</li> <li>(3) Payment of Stamp Duties and Fees.</li> <li>(4) Issue of Certificate of Incorporation.</li> </ol>	The promoters complete the various documents and forward them, together with a cheque for the various stamp duties and fees to the Registrar of Companies at Bush House. When the Registrar has satisfied himself that the requirements of the law have been duly complied with, the Certificate of Incorporation is issued. At this stage the Company comes into existence as a legal entity, though, in the case of the Public Company, it is not as yet entitled to commence business.
III. Raising the Capital.	<ol style="list-style-type: none"> <li>(1) First Board Meeting.</li> <li>(2) Adoption of Preliminary Contracts, etc.</li> <li>(3) Appointment of Bankers.</li> <li>(4) Application for Stock Exchange Quotation.</li> <li>(5) Registration of Prospectus.</li> <li>(6) Issue of Prospectus.</li> </ol>	The Company must now proceed to appeal to the public for subscriptions to the capital, and for that purpose it must issue a prospectus which must first be delivered to the Registrar of Companies for registration.
IV. Issue of Shares.	<ol style="list-style-type: none"> <li>(1) Receipt of Application by Bankers.</li> <li>(2) Allotment of Shares by Directors.</li> <li>(3) Posting Letters of Allotment.</li> <li>(4) Posting Letters of Regret.</li> <li>(5) Splitting Letters of Allotment.</li> <li>(6) Issue of Share Certificates (within 2 months after allotment).</li> <li>(7) Preparation of Register of Members.</li> </ol>	At this stage the directors receive the applications for shares from the public and make the necessary allotments. Unsuccessful applicants are notified by a "Letter of Regret." A further instalment on the shares is usually payable on allotment.
V. Commencement of Business.	<ol style="list-style-type: none"> <li>(1) Lodge Statutory Declaration in regard to— <ol style="list-style-type: none"> <li>(a) Minimum Subscription.</li> <li>(b) Directors' Qualification Shares.</li> </ol> </li> <li>(2) Issue of Certificate to Commence Business.</li> <li>(3) Issue of Statutory Report to Shareholders.</li> <li>(4) Holding of Statutory Meeting.</li> </ol>	A declaration is filed with the Registrar to the effect that the Minimum Subscription has been subscribed and that the Directors have taken up and paid for their qualification shares. Upon the issue of the trading certificate, the Company is free to commence business.



registered office. Notice of the situation of this office must be delivered to the Registrar within 28 days of the incorporation of the company, and within 28 days of any change in the address. As a rule this document is delivered on registration.

When these documents have been lodged and the necessary stamp duties and fees paid, the Registrar, after satisfying himself that everything is in order, will issue a *Certificate of Incorporation*. Upon the issue of this certificate the company comes into existence as a legal entity and, in the case of a private company or a guarantee company without share capital, may commence business. Once this certificate has been issued, the validity of the registration of the company cannot be called into question by any person. This again is but a common-sense protection for the commercial community, since the course of business would be rendered much more uncertain if it were possible, after a period of time had elapsed, to go back and cast doubts on the validity of the certificate of incorporation.

In the case of a public company, the issue of this certificate does not empower the undertaking to commence business. Before this can take place a statutory declaration must be filed with the registrar stating—

(a) That every director has paid, in cash, on the shares which he holds, the same proportion as the public must pay on application and allotment.

(b) That if the company has issued a prospectus to the public, shares have been allotted, payable in cash, to an amount equal to the minimum subscription.

(c) If no prospectus has been issued, that a statement in lieu of prospectus has been lodged.

Upon receipt of this declaration the Registrar will issue a certificate entitling the company to commence business, commonly known as a *Trading Certificate*, upon which the company may carry on its ordinary business.

**THE CAPITAL OF A COMPANY.**—From a legal standpoint, the capital of a joint stock company consists of that portion of the nominal capital as stated by the Memorandum of Association which has been issued to the public. Shares may be issued by a company either in exchange for cash or for value in any other form such as property or services. Thus, it frequently happens that when a new company acquires property such as an established business for



example, the vendor receives the purchase price from the company partly or wholly in the form of fully paid-up shares. Again, the promoters of a company may receive payment for their services in the form of shares. However, the bulk of the shares will usually be taken up and paid for in cash.

A company is under no compulsion to issue the whole of its nominal capital as stated in the Memorandum of Association. The amount which is actually issued to and taken up by the public is known as the *Subscribed Capital*. When shares are paid for in cash it is customary for the payments to be made by instalments, a certain proportion being payable when the shares are originally applied for, a further proportion when they are actually allotted, and the balance in one or more instalments. In this respect a company can make its own arrangements, the only reservation being that the amount payable on application must not be less than 5 per cent of the nominal value of the shares. The amount which has actually been paid is known as the *Paid-up Capital*, whilst the amount yet to be called up is termed the *Uncalled Capital*. In certain cases the regulations of the company may prescribe that this uncalled capital cannot be called up by the directors except in the event of the company going into liquidation. In this case it is known as *Reserve Capital*. Again, it sometimes happens that shareholders do not pay instalments on the shares which they hold when these are called for by the company. These outstanding amounts are referred to as *Calls in Arrear*. The relationship between these classes is shown in the diagram on page 169.

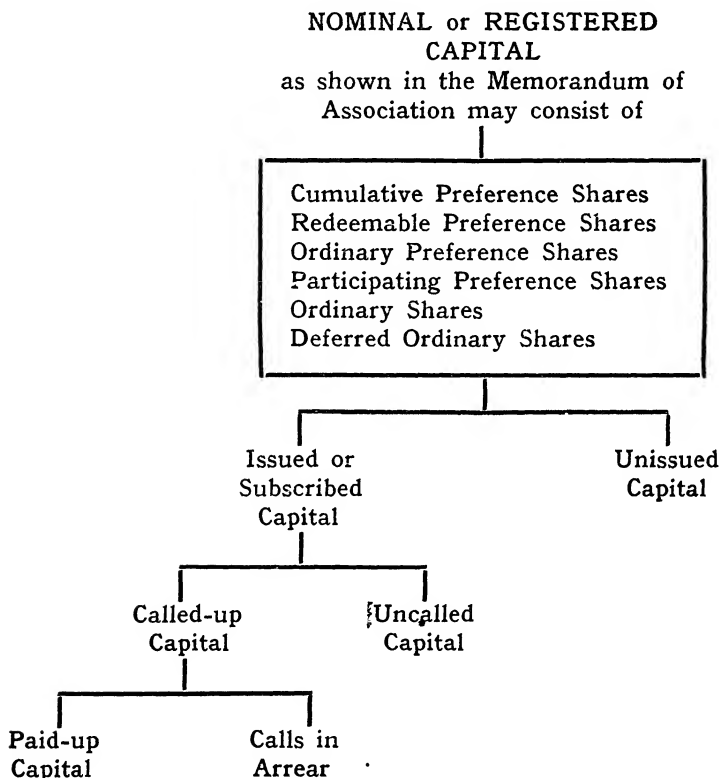
The issued capital of a company may be of a number of classes each of which carries its own distinctive rights. The chief of these classes are the following—

(1) **Ordinary Shares.** The holder of ordinary shares in a joint stock company might fittingly be described as a pioneer of industrial and commercial enterprise, since the greatest risks of the business usually fall upon his shoulders. He subscribes to the share capital of a business without having any special security for his investments other than his estimate of the inherent soundness of the concern, whilst he cannot claim any priority in the payment of dividends. Indeed, in both these respects, his rights are often subordinated to those of other classes of shareholders who can claim priority in the repayment of capital and priority to a share in the distribution of



profits. In return for these disabilities, however, the ordinary shareholder usually stands to receive a relatively high return on his capital investment in the years of prosperity when business is good

## THE CAPITAL OF A JOINT STOCK COMPANY



and earning power high. The ordinary share, therefore, may be regarded as an investment of a somewhat speculative type.

(2) **Preference Shares.** These shares are issued by a company and confer a preferential claim to dividends upon their holders, and very frequently a priority in the repayment of capital in the event of a winding up. Unlike the ordinary share, however, which has a right to dividends of any magnitude which the directors may care to declare provided that sufficient profits are earned to cover them.



the preference share usually carries a right to a fixed rate of dividend which must be paid before the ordinary shareholders receive anything. The preferential shareholder, therefore, receives his dividend and the ordinary shareholder takes the residue so that the preference shareholder obtains no benefit in times of good trade. In some cases shares are created known as *participating preference shares* in which preference shareholders can take dividends at a fixed rate, then ordinary shareholders may receive dividends up to a stated maximum and any residue of profits which may still remain available for distribution will be shared between the two classes in some specified proportion. The preference share is not quite so speculative in character as the ordinary share, though it must be emphasised that in either case no dividend can be declared unless profits have been earned to cover it. In some cases a class of *cumulative preference shares* is issued so that if preference shareholders do not receive their dividends in one year, the balance is carried forward and must be paid out of profits earned in subsequent years before any distribution can be made.

**Deferred Shares.** It sometimes happens that if an existing business is converted into a public company, the vendors of the business wish to retain powers of control and rights to a large share of profits in their own hands. They therefore create a class of deferred shares which they hold themselves. These shares usually carry special voting powers in meetings of the company and their rights to a dividend are deferred to those of the ordinary shareholders. Thus, it may be laid down that the holders of ordinary shares shall possess certain restricted voting rights and also a right to dividends up to a maximum of, say, 10 per cent. All profits in excess of this amount shall be distributed amongst the deferred shareholders.

**RAISING THE CAPITAL.**—Having registered the company at Bush House, the directors of a public company now set about raising the capital which they require by issuing a Prospectus. This is an appeal to the public usually published in the form of a circular or a press advertisement, inviting them to subscribe to an issue of shares, full particulars of which are given. Before the Prospectus can be offered to the public, a copy must be delivered to the Registrar of Companies signed by every director or proposed director mentioned in it. Now, since the Prospectus is the means whereby members of the investing public are induced to subscribe



to the share capital of the company, the Companies Act, 1929, lays down a number of requirements regarding its composition which are designed to check the activities of the unscrupulous. The drafters of the Prospectus are under the obligation of disclosing all material facts connected with the flotation of the company, i.e. all matters which might reasonably be expected to influence the decision of the average person to take shares in the company. Over and above this general duty of disclosure, the Act specifically names a list of matters which must be included.

The Prospectus may be issued to the public by the company through its bankers and any other medium by which publicity may be gained, or the whole business of issue may be given into the hands of an *Issuing House* which will deal with the whole of the technical details for a commission. In any case, the directors of a company cannot proceed with an issue of capital unless the amount of the Minimum subscription has been applied for, and if the subscription falls short of this amount the money must be refunded. In order to avoid difficulties of this type an arrangement is entered into with an *underwriting firm* that, in return for a stated commission, the underwriters will take up and pay for a certain number of shares if these are not subscribed by the public. The commission is, of course, payable whether the underwriter is called upon to take up the shares or not. This operates as a kind of insurance that the issue will be taken up.

**APPLICATION FOR SHARES.**—The prospective shareholder who, on the strength of the prospectus has decided to apply for shares in the company, must fill up an application form on the lines of the specimen on page 172. This form, together with a cheque for the amount required upon application, will be forwarded to the company's bankers. The completion of this form constitutes an offer on the part of an applicant to take up and pay for the number of shares stated or any smaller number that may be allotted to him by the directors. This offer is converted into a binding contract after the directors have posted their acceptance in the form of a *Letter of Allotment* to the shareholder. This document takes the form of a notification that a certain number of shares have been allotted and usually requires that a further instalment shall be paid within a stipulated time. If, however, the issue has been over-subscribed, that is, if applications have been received for a greater



## SPECIMEN APPLICATION FORM

No.....

### THE ENTERPRISE ENGINEERING COMPANY LIMITED

Issue of 750,000 Ordinary Shares of £1 each at  
20s. 6d. per Share

#### FORM OF APPLICATION

To the Directors of

THE ENTERPRISE ENGINEERING COMPANY, LTD.,  
37 Mount Stuart Square, Cardiff.

GENTLEMEN,

Having paid to your Bankers the sum of £...125....., being a deposit of 2s. 6d. per Share on application for .....1,000..... Ordinary Shares of £1 each of your Company (being 2s. per Share in respect of capital and 6d. premium), I/we apply for that number of Shares at 20s. 6d. per Share and request you to allot the same to me/us, and I/we hereby undertake and agree to accept such Shares or any less numbers that may be allotted to me/us, upon the terms of the Company's Prospectus, dated the 27th day of July, 19 . . , and subject to the Memorandum and Articles of Association of the Company, and I/we agree to pay the further instalments as provided by the said Prospectus, and I/we hereby authorise you to place my/our name(s) on the Register of Members of the Company as holder(s) of the said Shares.

Yours faithfully,

Usual Signature.....*Wm. J. Smith*.....

{ Surname..... *Smith* .....

{ Christian Name or Names.....*William James*.....

PLEASE  
WRITE  
DISTINCTLY { Address..... *210 Newport Road,*.....  
..... *Cardiff* .....

{ Profession or Occupation.....*Engineer* .....

{ Date.....*29th July* ....., 19 . ....

APPLICATIONS IN THE NAME OF A FIRM WILL NOT BE ACCEPTED.

Cheques should be made payable to "Midland Bank Limited," or "Bearer," and crossed "& Co." If altered from "Order" to "Bearer," the alteration should be signed by the Drawer.

An acknowledgment will be forwarded in due course, either by Allotment Letter or return of the deposit.



number of shares than are available, *Letters of Regret* are sent to the unsuccessful applicants and their application money is refunded at the same time. In the event of such an over-subscription, the policy pursued with regard to allotments is subject to some variation. The directors may eliminate all applications for less than a certain number of shares and allocate the remainder *pro rata*. Alternatively, if the business is such that a large number of shareholders has a publicity value, small applications may be allotted in full at the expense of large ones.

**TRANSFER AND TRANSMISSION OF SHARES.**—As already indicated, one of the principal advantages possessed by the investor in the modern public company lies in the marketable nature of the securities which he holds. One of the first steps taken by a newly-formed company will be to apply for a Stock Exchange quotation for its shares so that a market for them may be created. Any shareholder wishing to sell his holding must draw up a transfer deed on the lines of the specimen shown on page 174. This must be stamped at the rate of £1 per cent of the consideration passing, with varying amounts for fractions of £100. Every *transfer of shares* must be approved by the directors of the company, who usually reserve the right to reject transfers which they consider undesirable. When the transfer has been approved, the necessary alterations are made in the Register of Shareholders of the company and new share certificates are issued. Upon the death of a shareholder, the right to deal with his shares automatically is vested in his legal personal representative. The passing of the right of dealing with the shares to the legal personal representative is known as *transmission*.

**MANAGEMENT OF THE COMPANY.**—The registration of a company under the provisions of the Companies Act, 1929, calls into existence a new legal entity, capable of carrying on business, and of owning and disposing of property. Yet, such an impersonal creation of law must act through some human intermediary, who, in practice, takes the form of the company director. It would be a matter of impossibility for the shareholders of a large public company to exercise their rights as proprietors and manage the company's affairs personally, so that it becomes necessary for them to elect a variable number of representatives who can act for them. In practice, the mode of appointment of such persons is almost invariably prescribed by the Articles of Association, but Section 139 of



# SPECIMEN SHARE TRANSFER DEED

Certificate of the within mention 100 Ordinary Company's Offices by William Arthur Robinson.

*William Arthur Robinson,  
201 Penylan Road,  
Cardiff.*

in \*consideration of the sum of *one hundred and fifty pounds*  
paid by

*Robert James Hardcastle,  
174 Glebe Road,  
Bristol,*

hereinafter called the Transferee,

**Do** hereby bargain, sell, assign and transfer to the said Transferee—  
*One hundred (100) Ordinary Shares of One Pound each, fully paid,  
numbered 375,001 to 375,100,*

of and in the undertaking called

*The Enterprise Engineering Company, Limited*

**To** hold unto the said Transferee, *his* Executors, Administrators and Assigns, subject to the several conditions on which *I* held the same immediately before the execution hereof; and *he* the said Transferee, do hereby agree to accept and take the said *shares* subject to the conditions aforesaid.

**As Witness** our Hands and Seal, this *eleventh* day of *October*

In the Year of Our Lord One Thousand Nine Hundred and

Signed, sealed and delivered by the above-named

• *William Arthur Robinson* in the Presence of }  
Witness's { Signature *John Collins* } *Wm. A. Robinson* (Seal)  
Address *55 Cathedral Road, Cardiff*  
Occupation *Clerk*

Signed, sealed and delivered by the above-named

• *Robert James Hardcastle* in the Presence of }  
Witness's { Signature *William Smith* } *Robert J. Hardcastle* (Seal)  
Address *172 Glebe Road, Bristol*  
Occupation *Clerk*

Signed, sealed and delivered by the above-named

• \_\_\_\_\_ in the Presence of }  
Witness's { Signature \_\_\_\_\_ } \_\_\_\_\_ (Seal)  
Address \_\_\_\_\_  
Occupation \_\_\_\_\_

Signed, sealed and delivered by the above-named

• \_\_\_\_\_ in the Presence of }  
Witness's { Signature \_\_\_\_\_ } \_\_\_\_\_ (Seal)  
Address \_\_\_\_\_  
Occupation \_\_\_\_\_

\* The Consideration-money set forth in a Transfer may differ from that which the first Seller will receive, owing to sub-sales by the original Buyer; the Stamp Act requires that in such cases the Consideration-money paid by the Sub-purchaser shall be that inserted in the Deed, as regulating the *ad valorem* Duty. The following is the *Clause* in question—

"When a Person having contracted for the purchase of any property, but not having obtained a Conveyance thereof, contracts to sell the same to any other Person, and the property is, in consequence, conveyed immediately to the Sub-purchaser, the Conveyancer is to be charged with *ad valorem* Duty in respect of the Consideration for the Sale by the Original Purchaser to the Sub-purchaser."—[33 & 34 Vict. Cap. 97, sec. 74, sub-sec. 3.]

When a Transfer is executed out of Great Britain it is recommended that the Signatures be attested by H.M. Consul or Vice-Consul, a Clergyman, Magistrate, Notary Public, or by some other Person holding a public position—as most Companies refuse to recognise Signatures not so attested.

\* A WIFE SHOULD NOT WITNESS HER HUSBAND'S SIGNATURE, NOR SHOULD HE WITNESS HERS



the Companies Act provides that every company registered on or after 1st November, 1929, must have at least two directors, unless it is a private company. Upon the formation of a new public company, it is customary to insert in the Articles the names of the persons who are to be appointed the first directors. Subsequent appointments are usually made annually by the company in general meetings. Thus, in theory at all events, the directors are responsible to the shareholders for their conduct of the company's affairs, and their actions are subject to a measure of criticism and control of shareholders' meetings. Such control can rarely be said to be very effective, however, since the majority of the shareholders of a large company never attend the annual meetings.

**DIRECTORS.**—The principles on which directors are selected vary widely from one concern to another, but the trade depression has evoked a considerable volume of criticism against a number of common practices. Thus, there is the practice of selecting men of good social standing but with little or no knowledge of business to take seats on the board of directors. These are usually content to follow the lead of a dominating director, and "do not perform any function at all, but just sign where they are told to sign."<sup>1</sup> Occasionally such directors are appointed because of their ability to attract business to the company by reason of their influential connections. At other times they are appointed with the less laudable object of impressing the prospective shareholder with the standing of a new concern, and in such circumstances their appointment cannot be too strongly condemned. Cases have been far too frequent in which a director has lent his name to a company for what may be termed *window dressing* purposes, and has treated himself as thereby having given ample consideration for his remuneration, and as being absolved from any further effort towards promoting the welfare of the concern.

Moreover, so far as the duties of directors to the company are concerned, it has been clearly stated in the Courts that a director is not bound to give continuous attention to the affairs of his company. His duties are of an intermittent nature to be performed at periodical board meetings and at meetings of any committee of the board upon which he happens to be placed. So long as the

<sup>1</sup> Evidence of Mr. H. E. Burgess, Senior Official Receiver, before the Company Law Amendment Committee, Cmd. 2657, Minutes of Evidence, Q. 479.



provisions of the Articles of Association are observed, a director is justified in delegating duties to the paid officials of the company, and, in the absence of grounds for suspicion, is justified in trusting those officials. This, however, does not mean that his trust can be a blind one, for over-riding all else is the rule that he is bound to use fair and reasonable care and diligence in the discharge of his duties, and will be liable for negligence if he fails in this respect. With the exception of such powers as are vested in individuals or committees, the powers of control of directors can be exercised, as a general rule, only at a duly convened and properly constituted board meeting. A *board meeting* must be held in accordance with the principles laid down in the Articles, which may stipulate, for instance, that a meeting of the board shall be held on a specified day in each month. As a rule, however, the Board is convened as the requirements of business dictate. In order that it may validly transact business, the following conditions must be observed—

(1) All persons entitled to be present at the meeting should receive proper notice and have been given an opportunity to be present. The length of notice must be in accordance with the Articles and, in the absence of express instructions, must in any case be reasonable. Notice need not be given to a director who is abroad and out of reach.

(2) The proper person must be in the chair. As a rule the Articles provide that the directors may elect a chairman of their meetings and determine the period for which he is to hold office.

(3) If the articles stipulate the minimum number of directors who must be present in order to transact business, then unless this number is present any resolutions passed are invalid.

**MEETINGS.** Meetings of shareholders fall into a number of classes, the first of which is the *Statutory Meeting*. This is usually the first meeting of the shareholders of a joint stock company, and must be held not less than one month nor more than three months from the date at which the company is entitled to commence business. This meeting is convened in order to afford the shareholders an opportunity for seeing what degree of success has attended the flotation of the company, and in order that any special matters requiring their approval may be laid before them. The *Ordinary General Meeting* is the one at which the routine business of the company is transacted in the course of its ordinary operations and is usually very



sparsely attended. Such a meeting must be held once at least in every calendar year, and not more than fifteen months after the preceding ordinary general meeting. This meeting deals with such matters as the retirement and re-election of directors and auditors, consideration of the annual accounts, and the declaration of dividends. Thirdly, there is the *Extraordinary General Meeting*, which may be held subject to the terms of the Articles at any time the directors think fit when it is desired to transact business of a special character. Further, the directors must, on the requisition of the holders of not less than one-tenth of the paid-up share capital, convene an extraordinary general meeting. If they fail to do so within twenty-one days, the requisitionists themselves may convene the meeting, any reasonable expenses being paid out of the funds of the company.

**ACCOUNTS.**—The books which have to be kept by a company registered under the Companies Act, 1929, may be grouped under three headings—

(1) Financial Books which are essential for recording the transactions of the company according to the principles of double entry. Although the Act does not specifically state that the accounts must be kept on double entry principles, the requirements are such that they can be adequately covered only in this way.

(2) Statutory Books which are mainly books of record dealing with the membership of the company or its obligations and charges. They include a Register of Members, a Register of Directors or Managers, a Register of Mortgages and Charges, Minute Books, and an Annual Summary of Capital.

(3) Auxiliary Books which are not prescribed by statute, and are kept for purposes of convenience to facilitate the work of the company administration.

**AUDITORS.**—The appointment of an auditor at each annual general meeting to hold office until the next meeting is compulsory upon every limited company, both public and private. Directors and officers of the company are not qualified for appointment, since it is obvious that such procedure would not afford the members an independent audit.

The duties of the auditor are threefold—

(1) He must examine the books of the company.

(2) He must satisfy himself that the books disclose the true facts.



(3) He must report all material points to the shareholders. The auditor's report, duly signed, is attached to the balance sheet, and usually reads as follows—

*I have audited the above Balance Sheet and have obtained all the information and explanations I have required. In my opinion such Balance Sheet is properly drawn up so as to exhibit a true and correct view of the state of the Company's affairs to the best of my information and the explanations given to me and as shown by the books of the company.*

The Companies Act provides that the auditors of a company shall be entitled to attend any general meeting of the company at which accounts examined and reported by them are laid before the company, and to make any statements or explanations they desire.

### TEST PAPER XV

1. "In the field of economic organisation the development of the joint stock company is the most important constitutional development of the last century." Give a reasoned explanation as to why this should be the case.

2. With what limitations is a sole trader likely to meet as his business continues to expand? Explain how he may overcome these limitations by converting his business into a joint stock company.

3. What are the advantages, if any, of the joint stock company form of organisation as compared with the partnership?

4. What do you understand by a joint stock company? In what ways may a group of persons be incorporated according to English law? How does a corporation differ from a partnership?

5. The leading characteristic of capitalism can be put in the form of the proposition that "where risk lies there control lies also." How far is this statement true of the modern public limited company?

6. What is meant by an allotment of shares in a company? What statutory conditions must be fulfilled before an allotment becomes binding on the allottee of shares?

7. A company has a capital of £210,000 composed of £150,000 preference shares of £1 each, and 60,000 ordinary shares of £1 each. The preference shares are entitled to a dividend of 10 per cent per annum, and also to one-fourth of all surplus profits available for dividend after 20 per cent per annum has been paid on the ordinary shares; if the net profit for one year is £50,000, what will a shareholder receive who holds 3,500 preference shares?

8. Discuss the different ways by which a joint stock company raises its capital. What parts do the promoter and the underwriter play in the formation of joint stock companies?

9. The Cardiff Estate Company, Ltd., is formed to purchase a piece of land in Park Street, Cardiff, for the purpose of promoting a public company to run a dancing hall there. Frame a suitable objects clause for the public company to be promoted.

10. Explain the following terms in connection with a joint stock company: (a) Memorandum of Association, (b) Articles of Association, (c) Prospectus, (d) The minimum subscription, (e) Authorised capital, (f) Subscribed capital, (g) Issued capital, (h) Uncalled capital, (i) Reserve capital, (j) Calls in arrear, (k) Forfeited shares, (l) Directors' Minute Book.

11. What in your opinion are the principal functions of the Board of Directors and the Managing Director of a company?



## CHAPTER XVI

### ORGANISATION AND MANAGEMENT OF A BUSINESS

THE term "*organisation*" suggests a certain amount of calculated method and arrangement with a view to the production of better results than could otherwise be obtained.

The term "*business*" may be regarded as any form of activity connected with the making of profits. The organisation of business, therefore, has reference to a scheme of assigning duties upon some definite basis to persons engaged in a particular undertaking.

**NATURE OF ORGANISATION.**—The process of organisation is by no means a simple one, for it requires a high degree of skill to separate the work into parts and to allot each part to persons able to perform it. There is also the further difficulty of arranging for a supply of every kind of labour required ready to perform all the duties of any particular class, as and when the need arises. Moreover, the scheme of organisation must be so arranged as to find full employment for each class of labour.

One is apt to think of organisation, in connection with business affairs, as something analogous to machinery, a well-organised business being spoken of as running as "*smooth as a machine.*" This seems to imply that a scheme is thought out in advance, and, when once it is put into operation, it will work almost automatically. The idea that a business will work automatically, however, is erroneous, and when once a business is organised, it cannot afterwards be left to run by itself. The guiding hand and, still more, the guiding brain of the entrepreneur or organiser must always be there to direct it, and must be ready to formulate new plans where the original scheme fails to apply.

The term "*organisation*" is sometimes so used as to imply that all the thinking necessary for the execution of the work is concentrated in the brain of the organiser, and that matters are so arranged that subordinates have simply to do what they are told. This view is rather over-strained, however, for almost every kind of work performed by human beings requires some amount of attention, or it would probably be executed entirely by machinery.



Even if the thinking could be concentrated in one or a very limited number of individuals, there still remains the work of carrying out the programme thought out by the organisers, and this rests with the subordinates. It is, therefore, the organiser's duty not only to formulate a *scheme of organisation*, but also to see that the scheme is carried out ; and this is a vastly different matter. It is one thing to give instructions, and another to get the instructions carried out.

The faculty of getting one's instructions carried out is, primarily, a problem in psychology, and is one of the most important factors in successful organisation. The person whose duty it is to get the work done has to consider the material with which he is dealing. He has to consider the minds of those who are really to do the work, and then appeal to them so as to get it done.

One of the most difficult matters in connection with every complicated organisation is to arrange that all the various units of which it is composed shall work together so as to produce a definite result in the desired direction. Definite lines should be established upon which everybody is tending to work, with a view to avoid overlapping, and so to prevent the enormous waste of effort which must necessarily exist where there is a lack of understanding among all concerned.

**TESTS OF SOUND ORGANISATION.**—Whether an organisation be sound or unsound depends upon the efficiency with which it achieves the ultimate object of the whole enterprise. Organisation is not an end in itself; its purpose is to facilitate the task of achieving other goals. The following may be specified as the criteria of a sound organisation—

(1) **Ease of Execution.** The primary test of organisation is the degree to which it enables work to be executed economically and easily. A poor organisation is one in which the execution of work is unnecessarily complicated. In a sound organisation every essential activity is initiated and carried through with the minimum of trouble and the maximum of effect, taking into account all whose duties compel them to take a share in the activity.

(2) **Balance.** A sound organisation is one in which each branch of the business is equally effective, and is organised on a plan which conforms to the whole scheme. This may be called "organisation balance." If one unit of an organisation be well planned and one



poorly planned, the net result is an unsound organisation. Furthermore, if one unit be well organised for its own internal working, but be inadequately adjusted to other units, the result must again be unsound. It will be clear, therefore, that the effective organisation of a large concern, divided into many units, implies that every unit, whether it be a large or a small one, must be organised on the same principles.

**(3) Co-ordination.** A sound organisation is one which permits the full co-ordination of every branch, so that the performance of the work of each unit is economically related to the work of other allied units, and the whole complies with the requirements of the main policies of the business. To ensure this, the chief executive must hold within his own grasp the decision as to how the organisation shall be built up, so that it may regulate every extension and determine every change in the light of the plan which he is pursuing for the whole enterprise.

**(4) Capacity for Expansion.** A sound organisation is one which places the enterprise in a position to grow and expand, without dislocation, despite changes in the personnel or methods. An ideal organisation, if it is to be stable and secure, must provide for such contingencies. It is short-sighted to plan an organisation to fit the personnel, who may happen, at any given moment, to form the staff of a business.

**(5) Use of Labour Power.** A sound organisation is one which makes the fullest use of the available human power, to the satisfaction of the individuals comprising the organisation, and for their highest efficiency in operation. The art of organisation is to locate human beings in the structure so that each consistently contributes what is required of him towards the conduct of the whole undertaking. The organiser must recognise that men must be given complete jobs, carefully defined, if they are to feel a full sense of responsibility.

**FACULTIES OF BUSINESS ADMINISTRATION.**—The term “administration” is commonly used to describe in the most general way the whole of the activities involved in the control or direction of a business or similar enterprise. The conduct of a modern business, however, requires the exercise of many varied types of work, corresponding to different kinds of skill, and representing various techniques. Organisation consists of a combination of work-functions



with human faculties. Organisation, in fact, not only determines the nature of the work which a man is to perform, but also the faculty he is to exercise in that work. Thus, both the sales manager and the commercial traveller are concerned with the function of sales distribution, but the former usually exercises determinative or advisory faculties, whereas the latter employs mainly the faculty of execution.

### FACULTIES REQUIRED IN BUSINESS ADMINISTRATION

Faculty	Description of Personnel	Duties
Determinative	Board of Directors Managing Director	Determination of policy.
Administrative	General Manager Secretary Group Managers	General application of policy. Co-ordination between functions. Control of executive.
Executive	Departmental Managers Foremen Overseers	Departmental supervision and local co-ordination of function. Immediate supervision of work.
Operative	Factory Operatives Clerks Labourers	Manufacturing and functional operations.
Consultative	Apprentices Legal advisers Consulting Engineers Auditors Advertising Agencies	Specialised advice.

In every business undertaking, according to Sheldon,<sup>1</sup> the following faculties may be distinguished, though they may not be employed by separate persons—

(1) *Determinative Faculties.* It is impossible to consider the subject of organisation apart from the objectives which the particular enterprise aims to achieve. Before an organisation can be designed effectively, these objectives must be determined and defined. In other words, the business must have a “policy,” that is, a scientifically determined scheme, defining these objectives and governing the methods to be adopted in pursuit of them. The responsibility for the determination of policy lies with those who exercise the direction of the business. Thus in a joint-stock company it is the duty of the board of directors to exercise this faculty.

(2) *Administrative Faculties.* Under this heading we may place the faculties which control the general application of the business

<sup>1</sup> *Philosophy of Management* (Pitman).



policy. The management of a modern business comprises many different activities, and, as a business grows, the complexity increases. If a general policy is to be carried out effectively and economically, it becomes essential that means should be established for the co-ordination of all these activities. Buying must be made to link up with manufacturing, manufacturing with selling, selling with advertising, so that the whole force of these various branches may be brought to bear with the maximum of effect and the minimum of waste. The highest co-ordinating position is that normally held by a general manager or managing director. This position, by whatever name it may be known, stands midway between the board acting in a determinative capacity, and the management.

(3) *Executive Faculties*. Under this heading fall the broad group of activities which is usually termed management—the task, in general terms, of carrying out the policies of the business and of controlling and supervising the available means to that end. It includes all those who, in any degree, hold responsibility in the organisation—those who are usually designated as managers, foremen, supervisors, or technicians. They are executive in the sense that they are responsible for the manufacture of the firm's products, their sale to customers, the purchase of the necessary material, the advertising of the goods, and the keeping of the books. They execute these activities on the lines laid down for the general conduct of the business and exercise control and supervision by means of the organisation provided.

(4) *Operative Faculties*. This is the basic part of the industrial structure which is performed by the group we loosely call labour—the manual and mechanical work involved in manufacturing and distributing goods. This faculty is that which actually performs the task and applies the skill to actual operations.

(5) *Consultative Faculties*. Running through these grades comes the faculty known as Consultative. This faculty may be provided by specially qualified individuals, whether of the staff or from outside, or by the combination of individuals in committees. It is the faculty provided by works councils, inter-departmental committees, and the many conferences and meetings which form so distinctive a feature of modern organisations.

**MANAGEMENT OF A BUSINESS.**—Management includes the work of carrying out the policies of the business and of controlling the



available means to that end. The members of the managerial staff must control production, keep accounts, and maintain records and statistics of many varieties. They must purchase what is required by way of raw materials, plant and machinery, and devote attention to business research.

**THE STAFF.**—When a trader is unable to execute personally all the work involved in the transaction of his business, he appoints assistants, who are collectively known as the staff. The staff consists of those persons engaged in the business for the performance of commercial services in return for which they receive a money payment. The commercial staff must be carefully distinguished from those independent persons who are not under the direct control of the organiser (such as commission agents, brokers, etc.) and also from those who are engaged in rendering extractive or manufacturing services. The staff of a commercial house includes such members as the book-keepers, cashiers, salesmen, correspondents, warehousemen, travellers—in fact, every member of the concern, from the director in receipt of the highest fees, down to the youngest clerk with the lowest salary.

Persons who receive no reward for their services, such as the wife, children, or relatives of the employer, are not regarded as members of the staff.

The appointment of suitable persons as members of the staff is the basis of a proper system of division of labour, and is one of the chief factors in determining the success of an undertaking.

According to the particular activity engaged in by the respective members of the concern, the following persons may be distinguished—

(1) *The Book-keeper*, to whom is entrusted the control of the most important books for the record of trading transactions.

(2) *The Cashier*, who is responsible for the financial operations of the undertaking, and through whose hands all receipts and payments have to pass. He has to keep an account of all financial transactions, and is held responsible for the correctness of the balance as shown in the Cash Book.

(3) *The Correspondent*, whose duty it is to attend to the correspondence between the business of his employer and that of other business houses.

(4) *The Warehouseman*, whose duty consists in keeping the



warehouse in order ; receiving, examining, and stocking goods, executing incoming orders punctually, and according to instructions, and entering these various transactions in the warehouse books.

(5) *The Chief Clerk*, who is responsible for the keeping of the specialised books, or the execution of definite work in the counting house, such as the preparation of accounts, etc.

(6) *The Managing Clerk*, whose duty it is to distribute work among subordinates who are immediately responsible to him, and to supervise its execution. He may be the head of a particular department.

(7) *The Salesman and Saleswoman*, both of whom are in charge of the actual sale of goods.

(8) *The Authorised Clerk*, or person acting with full power of attorney, having unrestricted capacity to act for the principal. In particular he may—

(a) Accept bills of exchange and arrange loans on behalf of the firm.

(b) Buy and sell goods, open credit accounts, make payments, acknowledge or dispute claims.

(c) Enter into litigation in the name of the principal, and take the oath on his behalf.

(d) Rent or lease land, or redeem the mortgage thereon, or even acquire land on behalf of the principal.

(e) Employ or discharge employees, fix their salaries, and make out testimonials for them if required.

On the other hand, the Authorised Clerk is not generally empowered—

(a) To buy and sell land.

(b) To sell the entire business.

(c) To reconstruct or dissolve the firm.

(d) To sign Balance Sheets or to testify to the correctness of the stocktaking.

(e) To delegate to others the power of attorney.

When signing on behalf of the firm, the authorised clerk writes the words “per procuration ” or “per pro.” before the firm name and his own signature under it. His signature must be in handwriting, although the firm name may be stamped as follows—

PER PRO. JAMES HOWARD.

*Edwin Jones.*

A limited power of attorney may be given to the cashier to sign



bills of exchange for the firm, or to accept or refuse offers made by insolvent debtors. Again, a branch manager may be given authority to do all necessary acts, in his district, for the firm. It must be observed, however, that only those acts which such power of attorney authorises the agent to do are binding on the firm.

**Organisation of the Staff.** The staff of any business house, whether large or small, may be likened unto an organic body. That is to say, it consists of organs of various qualities, which are capable of performing very varied operations. The object of the organiser is to study the capacities of these different parts, to find out what each is best suited for, and, as far as possible, to divide the tasks to be performed so that each member of the staff may be given work which he is best able to do. An organised body differs from an unorganised body in the fact that specialisation of labour is carried out to the point when one part of the body is capable of doing certain things better than other parts, and, therefore, those functions are delegated to it to perform. On the other hand, unorganised bodies, even when they are living bodies, always represent a very low scale of development.

The organisation of the staff of a business undertaking, therefore essentially involves the distinction between different qualities, and a capacity to separate the tasks to be performed into parts or stages. The tasks are then delegated to persons possessed of different qualities, so that each may be working to the best advantage.

However, it is conceivable that the tasks in a business may be distributed on the above lines, but without any co-ordination between the various members of the staff. This would seriously hamper the execution of any constructive work, so that it is necessary to establish in a business, not merely an independence of the parts, but also an interdependence of the parts. If the tasks have been delegated to the members of the staff according to their particular qualities or capacities, and the undertaking has also been divided into departments with the most suitable person at the head of each, then there should be a proper system of co-ordination between the separate departments, so that the managers may be brought into constant communication with each other.

**ORGANISATION IN RELATION TO COMPLAINTS.**—Under ideal conditions, complaints ought not to exist, although in practice they do exist, and the proper method of dealing with them is a



matter of great importance, on account of the very far-reaching nature of the effects of causes which, in the first instance, seem to be altogether insignificant.

Complaints may arise from all sorts of sources, but, broadly speaking, they may be classified as coming from—

- (a) Customers.
- (b) Employees.
- (c) Outsiders.

The general tendency in many cases is not to make any attempt at organising this branch of business experience, probably under the mistaken impression that in so doing one would be encouraging its development. No such action on the part of the organiser of the business would multiply the actual number of complaints in existence. All that it would be likely to do would be to provide the means by which a great percentage of complaints which do exist might get to the knowledge of the manager. When persons are dissatisfied and think that they are badly treated, their minds should be disabused of the fact that the business management is quite indifferent about it and does not desire to provide a remedy.

In the absence of organisation to deal with complaints, the probability is that in the ordinary course of events any expression of dissatisfaction will really be made to the person primarily responsible for the fact that there is dissatisfaction. That is to say, the first, and very likely the only, effort to deal with the situation at all is made by some one who is, from the very beginning, more or less on his defence. His method of dealing with the complaint would be quite different from that of anybody else of equal intelligence. The mere fact that he is on his self-defence, that he looks upon the complaint as being made against himself, naturally predisposes him to hush it up, or to get rid of it with the least possible amount of fuss, and without his superior getting to know what has happened. Very naturally, in quite a number of cases he succeeds. What one never gets to know is the amount of harm done to the reputation of the business in achieving this personal success.

The first axiom to be laid down is that those who are responsible for the complaints are the last persons to be deputed to set them right. As a matter of fact, practically all complaints and all disputes are the result of mistakes. If the complaint is not well



founded, it has been made by the claimant under a misapprehension of the position, and, probably, if the true position could be explained, not merely all ground for complaint but all feeling that one had a ground for complaint would be removed. It is very little good attempting to deal with complaints save on the lines of first ascertaining what is the real cause of the annoyance—because there is always a feeling of annoyance when there is a dispute—and then dealing with it.

The person most suited for this work is the *manager* or managing director.

Even when a complaint is justified, it sometimes pays to concede a point, but it never pays to do this when the time for doing it effectively has gone by. It should be conceded quickly and gracefully, so that it may appear that some concession is being granted.

Again, if reason is exercised, and sufficient trouble is taken, there should be no difficulty in adjusting disputes with other persons, provided those other persons are also reasonable and straightforward. But if they are thoroughly unscrupulous people, it is quite likely that no headway will be made with them at all. Whatever is done for them, they will be unsatisfied. Their whole position is an attempt to get something to which they have no right. The more they think they can get, the more they will persist in putting forward their claims. One should avoid, as far as possible, having any dealings whatever with such persons, and although it is difficult to know in advance who comes under this heading, when once they are found out they should be left severely alone.

#### TEST PAPER XVI

1. What do you understand by the "organisation of business"?
2. Where there are several departments in a business, how can overlapping be avoided?
3. What is the meaning of the "Staff" in connection with a business?
4. Enumerate six persons who are usually important members of the staff.
5. Explain the function of the "Authorised Clerk," and state the nature of the power which is usually conferred upon him.
6. Give an illustration of the manner in which the "Authorised Clerk" should sign on behalf of a firm.
7. How may complaints arise in business?
8. Do you think the manager of a business should concern himself with customers' complaints?
9. Outline a scheme for the general organisation of any business with which you are acquainted, from the principal or principals down through sectional managers to the general staff.
10. What are the principal aims of business organisation? What tests should be applied to ascertain whether a given organisation is satisfactory?



## CHAPTER XVII

### THE MODERN OFFICE

CHANGES and improvements are daily taking place in the conduct of business concerns. The influence of a higher standard of education, the extension of commercial operations, the rise of large-scale undertakings, together with the accompanying division of labour, have all materially conduced to raise the question of business organisation to a higher plane. To this end, and that of attaining the highest efficiency, have been applied numerous inventions of all kinds, as well as the investment of much capital. In this chapter, one aspect of this progress will be seen in the description of the modern office.

**GENERAL ORGANISATION.**—In former days, any dark, dingy room used to serve as office ; but, to-day, generally speaking, the demand is for spacious premises and bright surroundings, especially in the case of large undertakings, in whose service hundreds of clerks are often employed.

The modern office is usually situated in a palatial building of three, four, or even more storeys in height, a special section being allocated to the Book-keeping staff, one to the Correspondence staff, another for the office of the Cashier, and one for the Forwarding or other departments. Just as the whole business is grouped into departments, so each department undergoes a similar division of functions. In many large undertakings, there are as many as 100 different departments, each in possession of its own particular office. In addition to the particular rooms allocated to the different departments, provision is sometimes made for Receiving and Waiting Rooms, Telephone Room, private offices for the various Managers, Postal and Telegraph Rooms, as well as other rooms of minor importance.

In the offices themselves, order and cleanliness usually prevail ; throughout the day a stream of light pours into the building through the high, broad windows ; whilst at night, electric light sheds forth its rays ; and in winter, electricity serves for heating purposes, spreading a pleasant warmth throughout the entire place.



In the offices themselves, the desks are so arranged that each employee can work undisturbed along with his colleagues. In the case of cash and other dealings with the public, there are special counters or places of inquiry, so that a speedy service is possible even at busy times. In the office of the managing director, one is astonished to see, not only the artistic and tasteful arrangement of this important room, but also the perfect order in which it is kept, for it is from this centre that the various branches of the business are brought together into one thread, and from which the dominant influence of the chief is exerted in every direction. One is apt to wonder how a single brain can direct and control such a large undertaking. It is sufficient here to point out that every large commercial concern is built upon a carefully designed scheme, which is the outcome of much reflection and many years of experience. In addition, there is a general scheme for the organisation of the workers in each department, and duties and responsibilities are delegated to each particular manager, who, in turn, allocates the special tasks for the employees who are subordinate to him. Each member of the whole organism not only has his sphere of duty exactly prescribed him, but—what is of greater significance—has sufficient scope left for his free play of initiative. Thus, two objects are achieved—

(1) The work is systematically arranged like the wheelwork of a watch.

(2) The thousand-and-one new duties and developments which frequently occur in a commercial concern can be undertaken by those who are able to assume responsibility for their execution.

In this latter respect is to be found the great difference between the employee who is reflective, conscientious, and self-reliant, and the unreflecting mechanical worker. The former not only makes himself thoroughly acquainted with the particular sphere of duty delegated to him, but endeavours to bring into proper perspective the entire business, with its many ramifications, and thus proves himself competent to execute more important duties in the interest of the concern. On the other hand, the latter remains an unskilled labourer, who merely does what he must, or what he is instructed to do. This usually means that his work is of a purely mechanical type and that he is paid a salary which is correspondingly low.



**FUNCTIONS OF THE OFFICE.**—The office is that part of a business enterprise which is devoted to the direction and co-ordination of its various activities. It is the seat, not only of the administrative activities which determine the policy of the whole business, but also of the principal executive activities whereby that policy is carried into effect. In certain types of enterprise, the importance of the office is evident, since it is the only visible embodiment of the business which is carried on, as in the case of banks and insurance companies. It is possibly partly for this reason that these institutions have devoted an unusual amount of attention to the construction and equipment of their offices. In other classes of enterprise, however, the office has usually suffered in comparison with the factory, being regarded as a necessary evil which must be tolerated but not encouraged. The false and vicious conception which, even to this day, has led so many people to stigmatise the office worker as “unproductive” has cramped the activities of the office and has thereby impaired the efficiency of the business as a whole. Office management has not been considered in the past as in any degree an important factor in the business, so that scientific developments have been slow and have by no means kept pace with those in the operative departments. In recent years, it is true, there has been a tendency for this attitude of mind to die out in favour of a more enlightened conception. The growth in the size of the business undertaking which has occurred in so many industries is preconditioned by effective managerial control. This can never be secured if the office organisation is defective, and consequently much-needed reforms have been introduced.

The importance of the office organisation in the efficient management of the business may be gained from a consideration of the following functions discharged by it.

(1) **Correspondence.** In many businesses a large proportion of the transactions which are effected with outside concerns are conducted through the medium of correspondence. Starting with the incoming correspondence, which forms the foundation of the work of many of the departments, a system has to be organised for examining and distributing it to the executives who have to deal with it, and for securing that all matters contained in it receive due attention. In like manner efficient arrangements must be made for dealing with the outgoing mail so that all inquiries receive prompt attention.



It should be remembered that the letters which are sent out are the "silent ambassadors" of the business, and should therefore be prepared with a view to making the best possible impression. Again, in connection with the Sales Department, a considerable amount of circularising may have to be done, involving the production of letters in bulk. For this purpose considerable use may be made of mechanical devices in order to minimise labour and save time. In a large concern there is likely to be a considerable amount of inter-departmental correspondence as well, since it is a safe rule to follow that any information or instructions passing from one section of the business to another should be put in writing in order to minimise the possibility of errors. A system of messengers or conveyors must therefore be instituted for dealing with this "internal" mail.

(2) **Financial Accounting.** This has long been recognised as one of the principal office functions—indeed, at one time, book-keeping was widely regarded as the only function of any consequence performed by a clerk. Formerly it was sufficient if the person entrusted with the supervision of this section could balance his books accurately, and take out the final accounts and balance sheet. To-day, however, much more is demanded of the accountancy function. With the growth of business it has become realised that the accounts represent a great storehouse of information which, in skilful hands, can yield most valuable guidance in the shaping of business policy. Competition has constantly grown keener, and in many cases a fractional percentage can mean the difference between profits and losses. Prices and profits are shaded so finely that one bad line can swallow up the profits on twenty good lines. It is therefore essential at the present day that the directorate should be in possession of such figures as will enable them to know at once how and where sales are being made. Such results could never, in a large concern, be produced by the old methods, and in this sphere mechanical methods have invaded the office with conspicuous success. They enable this most exacting work to be discharged with both speed and accuracy.

(3) **Cost Accounting.** Under present-day conditions, the information disclosed by the financial accounts, even in the more comprehensive form mentioned above, is insufficient. The financial accounts deal with aggregate values for the most part and do not reveal the details of the elements which go to make up these values.



This additional information is furnished by the costing system, which endeavours, as far as possible, to localise profits and losses, and to connect them with the transactions to which they are due. Indeed, a standard work on accounting has described the usual statement of profit arrived at without costs as "undiscovered differences in the books of account." Those who ignore the call for cost accounts are cultivating and increasing the speculative element which is present to a certain extent in every business. Accurate costs are, in these competitive days, of vital importance, because in keen competition an incorrect estimate of cost may mean either the loss of an order to a competitor or loss of profit if the order is secured, for it is very largely on the experience of past costings that estimates are prepared. Hence it will be the function of one section of the office staff to analyse the various items of works expenditure—materials, labour, and overhead charges—in such a way as to ascertain the cost of executing any given piece of work. In certain cases, such figures are readily compiled on the basis of the financial accounts, but in other instances a very elaborate analysis may be called for. In either case, however, the two systems should be linked together, since, after all, they are dealing with the same facts, though from different angles.

(4) **Statistical Control.** In addition to the financial and costing records, it is now recognised that the executive of a large commercial or industrial concern must be provided with appropriate and reliable statistics. Much of this statistical material will be derived from the same sources as the foregoing, but will in addition include many matters which are not considered in the accounting records. In any case, however, the aim of statistical technique is to present facts in a compact form so as to make them disclose readily the maximum amount of information. The office should be prepared to furnish statistical reports on such matters as—

(1) The detailed expenses of the business displayed so that comparisons may be made.

(2) Movements of stocks of raw materials and finished products showing details of individual lines.

(3) Effects of advertising campaigns showing the cost and relative efficiency of different media.

(4) The efficiency of travellers and agents as measured by the relation of their expenses to sales turnover.



(5) Surveys of the factory order book, showing which departments are busy and which are slack.

(6) The effects on profits or losses of a restriction of output or an increase in production to meet lower selling prices.

This list could be extended at considerable length, but sufficient indication has been given of the type of data which may be called for. In addition to these statistics relating to the internal economy of the business, a variety of external statistics may be collected for purposes of market research and similar matters. In such circumstances resort must be had to Government reports, figures issued by trade associations, newspapers, or the results of private investigations.

(5) **Administration.** As already indicated, the office is the centre from which the policy of the business is determined, and to this end all the above records are utilised. One of the most important duties of the office under this heading is that of planning the activities of the concern for considerable periods ahead. With the many complex elements at work in modern economic society, such planning is difficult, but the competent interpretation of economic statistics makes it possible to look ahead with a decreasing probability of error and with an increasing certainty that the plant will be kept regularly occupied. When the heads of the concern have arrived at these general decisions, the executive staff in the office must plan the actual output. Herein lies the work of production control. It covers the initiation of orders for raw materials, the issue of working instructions, the dispatch of materials through various processes, and the stocking of parts and of finished goods. Detailed plans are prepared for the most effective utilisation of men, machines, floor space and materials. In like manner, on the selling side plans are made for advertising campaigns, for the opening up of new territories by salesmen, and for undertaking market research. On the side of financial administration, measures must be taken to control the capital resources of the concern in order to utilise them in the most productive manner. These activities of the office are fundamental to the prosperity of the business.

(6) **Preservation of Records.** As we have seen, much of the work of the office centres about the compilation of records which it is essential to preserve if the time and effort expended upon their preparation are not to be wasted. It is therefore necessary to



safeguard them from physical destruction and to be able to locate them easily in case of need. For this purpose a wide range of filing systems and equipment are available, some details of which are discussed below. In this connection it must be remembered, however, that failure to follow a prescribed routine will cause the most elaborate system to break down. The work of filing and preserving business records is a responsible duty, and is not one which can with safety be entrusted to inexperienced juniors, as is so often the case. In a big office the work will be performed by a special section, and measures will be taken to keep track of records when they are removed from the files.

**MODERN OFFICE MACHINERY.**—In modern large-scale undertakings it is usual to find a whole series of machines and appliances designed to facilitate the execution of office work. The following is a brief survey of the most important types found in a large manufacturing business—

### MODERN OFFICE MACHINERY

#### I. Correspondence and Order Department

- |                         |                        |
|-------------------------|------------------------|
| 1. Telephone.           | 5. Letter Copier.      |
| 2. Typewriters.         | 6. Rotary Copier       |
| 3. Stamping Machines.   | or Roneo Duplicator.   |
| 4. Addressing Machines. | 7. Dictating Machines. |

#### II. Accounts Department

- |                                     |                                 |
|-------------------------------------|---------------------------------|
| 1. Elliott-Fisher Invoicing Machine | 2. Elliott-Fisher, National, or |
| (5 copies):                         | Burroughs Accounting            |
| (a) First copy to Customer.         | Machine.                        |
| (b) Second copy to Storekeeper.     | 3. Comptometer.                 |
| (c) Third copy to Accounts Dept.    | 4. Burroughs Adding Machine.    |
| (d) Fourth copy to Order Dept.      |                                 |
| (e) Fifth copy to Costing Dept.     |                                 |

#### III. Costing Department

1. Hollerith Punching Machine.
2. Hollerith Sorting Machine.
3. Hollerith Tabulator.

**TELEPHONE IN THE MODERN OFFICE.**—An important aid in the service of the modern office, which facilitates systematic control, is the telephone. In the office of a large concern there is usually a special telephone room, the charge of which is entrusted to a particular employee, whose duty it is to direct the incoming



messages to the right persons and also to link up with each other the various rooms within the same building.

To the desk of the managing-director is attached a telephone, by means of which he is enabled to converse, not only with his chief assistants engaged in the various departments of his business, but also with firms outside in the same town, or even with correspondents resident in distant parts of Britain or of the Continent. In this way, the head of the business enters into communication from his desk with his staff, as well as with his customers both near and far. Moreover, he gives and accepts orders, makes and receives inquiries, and is thus acquainted with every important movement in the World Market in the most convenient and quickest way. Hence, in an active and passive sense, he must be included as a link in the great net of world communications.

**STENOGRAPHY.**—Shorthand is not only of great importance in Parliament, public gatherings, and other meetings, but also in the commercial office. The head of the business has his chief correspondent at his side, and dictates to him the replies to the various letters which cannot be attended to directly by the procurists. The correspondent takes down in shorthand the dictation as fast as it is spoken by the chief, and his transcript is then made in ordinary writing. A similar procedure is followed also by the procurists in the execution of their correspondence through their subordinates. The employer who desires to have on his staff intelligent and self-reliant correspondents will take care not to make them slaves to the words spoken by him, but will allow them ample scope for initiative in the preparation of their transcripts.

**TYPEWRITER.**—The typewriter is used more and more widely every day in the commercial world, and those business concerns in which it has not been adopted are now the exception rather than the rule. It has three outstanding advantages—

(1) With the aid of a typewriter, the efficiency of a correspondent is increased threefold.

(2) It supplies a style of writing which is pleasing to the eye and easy to read.

(3) As many as twelve copies can be taken at each single operation of the machine.

Typewriting is an accomplishment which can be brought to



perfection only after considerable practice. In some districts it is customary for the correspondent to buy his own machine, so that he can take it with him into any new situation. In this way, he has the advantage of always being able to operate the same machine, and thus avoid the necessity of becoming acquainted with a different machine when entering another office.

**CALCULATING MACHINE.**—One of the most ingenious inventions of recent times is undoubtedly that of the Calculating Machine. By the aid of this device, all kinds of mathematical calculations, involving subtraction, addition, multiplication, and division, can be accurately and speedily performed, whilst its manipulation is easily and quickly learned. Although this machine is somewhat expensive, it is none the less coming into more general use. Since a complete reliance can be placed on its results, it not only saves an enormous amount of labour, but also simplifies the work of the calculating staff.

In large retail undertakings, an *Adding Machine*, or Cash Register, is often used for checking the cash takings. The machine not only gives a receipt for each item of money taken, but it—

(1) Shows everyone in the shop the amount of the sale and the initial of the assistant serving.

(2) Prints these particulars on a detail-strip, which is under lock and key.

(3) Prints and issues the receipt, showing amount of sale, initial of assistant serving, consecutive number, date, and any advertising matter on the back or front.

(4) Adds all the sales into one grand total.

(5) Shows at the close of the day's business the number of customers served, which assistant waited on each customer, the total of sales, and also gives a printed record of each sale on the detail-strip.

At the close of the day's business, it is an easy matter for the chief to read off the amount of cash takings and to compare this with the actual cash in the till.

**DICTATING MACHINES.**—The phonograph, originally used for the reproduction of songs, pieces of music, and speeches, has also been introduced as an office appliance. In composing his correspondence, the chief speaks into a special apparatus, the spoken words being preserved on a cylinder, which is afterwards brought into the



Correspondence Office. Here it is placed by an experienced typist into a second apparatus, when the correspondence is repeated clearly and slowly by the machine so that it can be written down by the typist. Should a sentence be misunderstood, the cylinder can be pushed back, in order that the words can be repeated and the letter correctly typed. Moreover, when once used, the cylinders can be put through a special process to fit them for further use.

**MODERN COPYING PROCESSES.**—Large commercial undertakings which receive and dispatch daily hundreds and even thousands of letters can no longer make shift with the old-fashioned copying press. Its place has been taken by the *Copying Machine*, which, within an hour, can produce as many as a thousand copies. Moreover, as many as five or six good copies can be taken from one typewritten or handwritten letter, if written with ordinary copying ink ; and if strong copyable ink is used, as many as thirty to forty copies can be taken.

The letters to be copied are laid on the feed-board, the handle is turned, the sheet is fed automatically into the machine, and a perfect copy is taken. This is repeated at the rate of twenty to thirty per minute as often as there are letters to be copied, the machine feeding in the sheet, making the copy, and storing it on the roll. A single copy, or seventy copies, can be cut off with automatic precision by one movement of the lever. The machine is simply built, constructed to carry a roll of specially-prepared paper, and requires no water. Every copy is of uniform size, and admits of easy filing and reference.

For each firm with which there is a continuous correspondence, a special portfolio is kept, in which all the incoming letters and copies of replies thereto are placed. The remaining task is so to preserve these portfolios that they can easily be found when required. This is rendered possible by the provision of a cabinet fitted with drawers. These drawers, as well as the portfolios contained therein, are arranged in alphabetical order, so that the correspondence with any particular firm is always at hand and can easily be referred to.

**PREPARED PRINTED FORMS.**—Business letters and correspondence can often be divided into certain groups in which the same sentences are constantly recurring. Merchants have, therefore, resorted to the practice of standardising such letters, etc., in printed form.



Under these circumstances, the entire work of correspondence consists in adding the address and signature, and the insertion of a few words or figures. By the use of such printed forms, the conduct of the correspondence is considerably furthered and facilitated. Very often the address is also printed on the envelope. When a business carries on a regular correspondence with a person or firm, the envelopes can be prepared on which the address is printed. These envelopes are kept in drawers alphabetically arranged, and on the dispatch of a letter an envelope is taken from the particular drawer. Another method is to print the frequently occurring addresses on gummed strips of paper, which are stuck on the envelope when required.

**DUPLICATING PROCESSES.**—In some cases, the correspondence is such that the same communication has to be addressed to many different persons. Such communications may be printed or lithographed, but this method is usually too lengthy and costly for the modern merchant. Hence a large number of duplicating processes have been introduced into the commercial office, such as press copying, gelatine process, carbon copying, and stencilling. Very often the typewriter is used as a duplicator. The letter is typed on a prepared sheet, which serves as the original, and after being fixed in a special apparatus, it is used for the production of innumerable copies. Probably the most suitable process of obtaining multiplex copies of documents, whether handwritten or typewritten, is by means of the stencil. The Mimeograph, Ellam's Duplicator, and the many rotary machines are all on the principle of the stencil. In preparing handwritten stencils, the writing is done by a stylus, on a prepared sheet. This sheet rests on an engraved plate, and in the process of writing with a stylus it becomes perforated, thus forming a stencil. When completed, it is firmly placed in a printing frame, beneath it being a piece of paper on which the impression is to be produced; a uniformly inked roller is passed over the stencil, and this forces the ink through the perforations on to the paper beneath, an exact copy of the original being thus made.

**CONTROL OF INCOMING AND OUTGOING CORRESPONDENCE.**—In order that the chief may know that each incoming letter has been answered and that the information in connection therewith has been properly entered up into the books of account, the whole



of the proceedings in connection with the correspondence must be systematically organised.

The incoming posts are attended to by one of the chiefs, and in some offices the letters are entered into a register known as an Index Book, and then distributed to the respective departments concerned. The departmental head then attaches to each letter received by him a label on which he states what has been done in connection with that particular communication. This is repeated in the various departments through which the letter is passed. Finally, it is examined by the chief to see that everything has been attended to prior to being filed.

**METHODS OF FILING.**—As already indicated, one of the most important of the duties of the office staff is that of preserving business records. At the outset, however, it is necessary to make a distinction between records which are of permanent value and those which are of purely temporary interest. This distinction is of some considerable practical importance, for, unless it is observed, the filing system will rapidly become encumbered with useless documents, which make excessive demands upon the available space, and cause delay in locating material which is wanted. This is particularly liable to occur in the case of correspondence files, and these should therefore be overhauled at regular intervals by some responsible person and all unwanted material eliminated.

The *aim* of a filing system is to provide a mechanism whereby business records may be stored so as to be readily available when required. The system must be adapted to the business and the purpose in view, and, generally speaking, it should conform to the following principles—

- (1) It should be as simple in its details as is compatible with the performance of the work expected of it.

- (2) There should be the least possible delay in gaining access to the records.

- (3) It should make provision for considerable expansion without dislocation.

- (4) It should be such that mistakes in filing are difficult to make and, if made, easily detected.

- (5) It should provide the maximum degree of safety from damage.

There are four important methods of filing worthy of consideration—



(1) **Direct Alphanetic Filing**, by name, as if arranged for a city directory. This is the most direct method of finding and filing papers.

(2) **Numeric Filing**, by arbitrary numbers assigned to each firm or subject. This system ensures the greatest accuracy, and is a virtual necessity where the subject-matter requires much cross reference.

(3) **Geographic Filing**, by names of towns. This system is usually designed for a business where territorial grouping is of leading importance.

(4) **Subject Classification Filing**. This is a classified numeric system by which papers are so arranged by correlated subjects that related matter is grouped in numeric order.

After the *outgoing* letters have been compared with the corresponding incoming letters, they are signed by the chief. Particulars are next entered into the Postage Book. If necessary, a copy of the outgoing letters is handed to the Accounts Department, where any items may be entered from them. Thus, by means of the two registers—one for incoming and the other for outgoing letters—there is always proof available as to whether a firm has received or sent a letter.

**A GENERAL SYSTEM.**—The following is a digest of a system of filing which can be varied to suit conditions, and used in part or in whole, according to the nature of the business. It is an adaptation of the vertical file which has been found to be the most satisfactory by the largest houses—

(1) All correspondence should be filed in folders and placed in vertical drawer files.

(2) If more than one file is kept, the name of each file or the drawer to which it belongs, should be written or stamped on each folder.

(3) The method of filing should be adapted to the business; for instance, one prominent house files retail correspondence alphabetically, wholesale correspondence geographically, and the advertising department correspondence numerically.

(4) The number of divisions the alphabet would be divided into in order to obtain quick reference depends upon the size of the correspondence; 20 subdivisions, 80 subdivisions, or even 240 subdivisions can be had.

(5) Each regular correspondent should be given a folder.

(6) Letters from casual correspondents should be placed in a "Miscellaneous" folder.



(7) With the numerical system of filing, guides with tabs projecting about half an inch should be placed at regular intervals to facilitate the finding of any desired number quickly.

**FOLLOW-UP SYSTEMS.**—The follow-up file or index is of value wherever there are duties to be performed in the future.

An inquiry is received about some article we are selling and we reply to it. If no answer is received we may wish to write again in ten days' time; the follow-up system will bring this to our notice at the proper time without taxing our memory in the least.

There are various systems, all of which are more or less a variation of one. Only three things are necessary—

- (1) Small cards on which to record the data.
- (2) Guides behind which the cards are to be filed.
- (3) A file in which to keep them.

Let us suppose a letter to which we reply is received from Mr. Smart on the 15th June. If, in ten days' time, we do not receive a reply, we wish to write again; on an ordinary record card we write Mr. Smart's name, the subject, together with the date of our letter. On the card we also indicate the date—June 25th—on which we wish the matter brought to our attention again. Coloured guide cards are used in the file. One coloured guide is marked one for each month of the year; another coloured guide is marked one for each day of the month. There will thus be a guide card marked JUNE; behind this will be thirty smaller guide cards of a different colour marked respectively 1–30. It is on the 25th June we wish to refer again to Mr. Smart's card. The record card on which we have written the particulars is placed behind the guide card which is marked 25. On 25th June all the cards which require attention on that date will be found behind this guide. Mr. Smart's card will be taken out; the file will be looked up to see if a reply has been received; if so, it will be noted on the card and filed ahead again, if desired, or destroyed, as the case may be. If no reply has been received, a second letter is sent, which we indicate on the card; it is then filed ahead another ten days, i.e. behind the fifth guide card at the back of the July guide, on which date it will come again to our notice. This system may be expanded or varied to almost any extent to meet the most varied requirements.

**CARD INDEXING.**—A transformation has taken place in the internal organisation of the office by the introduction of an



American system known as the Card Index. Its main feature is that certain kinds of business transactions are no longer entered into books, but are entered on cards. The cards are obtainable in any quantity and of uniform size; they may be coloured differently according to the purpose in hand. These cards were first used in connection with libraries. A ticket was made out for each book in the library, the name of the author, the contents of the book, and reference to the section of the building in which the book was preserved being given. Each ticket represented a definite book, and all the tickets together constituted a catalogue of the library. It was found to be more useful, however, to have two such catalogues—one in which the tickets were arranged according to the name of the author, and the other according to the contents of the book. Thus, if a reader desired the book of an author known by him, he would resort to the first catalogue. If he desired a work upon a certain subject, he would resort to the second catalogue. In recent years, this system has been developed and its countless applications have, with great advantage, been introduced into the service of the office. One of its most common uses is in connection with correspondence. One card is made out for each correspondent, bearing name and address and number of that correspondent's folder in the cabinet. This card is filed in an Index Box, alphabetically. To find the number of the folder, drawer, etc., containing any desired correspondence, reference is made to the index card, which latter, when once made out, indexes a correspondent for all time.

For instance, suppose it was necessary to refer to correspondence received from the Western Hardware Co., Bristol. We should first consult the card index, where, under the letters *We* following the guide card *W* we should expect to find the file number of the Western Hardware Co. (see illustration). The filing cabinet is then resorted to, and the drawer opened which contains the required file. This would probably contain in chronological order all the correspondence from and to the Western Hardware Co. for the last six months. As the latest communication would be on the top the letter or document required would be readily accessible. When the cabinet is full, the files are stored away in their numerical order and new ones, bearing the same number, are placed in the cabinet.

An additional advantage of the card index is that it provides a



complete list of addresses of all persons or firms with whom business is transacted. Further, memoranda may be made on the index card, thus supplying condensed information concerning the person or firm it represents.

**MODERN BOOK-KEEPING EQUIPMENT.**—In no section of the office has business practice been more deeply affected than in the Accounts Department in recent years. At one time, all the accounting

### CARD INDEX

Name <i>Western Hardware Co</i>		File No <i>1113</i>
Address <i>George St Bristol</i>		
Subjects <i>Hardware</i>	Remarks	
<i>Sporting Goods</i>		
<i>Stoves</i>		
<i>Agg. Implements</i>		

records were confined to cumbersome bound books, entries being laboriously copied from one to another by hand. This process was slow and therefore expensive, whilst errors were frequent and hard to detect. The extraction of statistical information required an elaborate analysis of the books of original entry, and by the time the figures were available their value was considerably discounted by the lapse of time. One of the first important steps towards the introduction of greater flexibility in accountancy systems was the development of the *loose-leaf* book. At first this device made but small headway, partly on account of a fear that it would lend itself too readily to the falsification of business records, and partly because of a fear that such a record would be inadmissible as evidence in a court of law. Subsequent developments have shown these fears to be groundless. Provided that loose-leaf sheets are kept under proper control there is little scope for malpractices on the part of



the clerks in charge of the ledgers. From a legal standpoint, the fact that sheets are bound in a book does not enhance their value as evidence, and in court accounting entries, if disputed, would in any case have to be substantiated by other evidence. The following advantages may be claimed for the *loose-leaf system* as compared with the bound book—

(1) The ledgers are not burdened with “dead” accounts, since these may be taken out and filed separately. At the same time it does not contain numerous blank pages arising from a miscalculation as to the space a particular account will occupy.

(2) New leaves may be inserted as required so that the book is “perpetual.” This obviates the tedious work of transferring accounts to new ledgers—and also avoids the risk of error entailed by such transfers.

(3) The loose-leaf ledger can be made self-indexing, since each account can be arranged in its allotted position, whilst guide sheets with projecting index tabs facilitate the location of a particular account.

(4) All the sheets relating to a particular account are to be found together, so that references to other parts of the book are avoided. At the same time, if the number of “live” accounts increases, the ledger may readily be subdivided.

(5) The work of posting, rendering statements, and of balancing can be divided amongst a number of clerks in order to speed up the work, whilst such loose leaves lend themselves to mechanical accountancy methods.

Systems of mechanical accountancy have, however, led to a further development in recent years—the *card ledger*. In order that the greatest benefit may be obtained from these systems, it is necessary that the minimum of time shall be wasted in handling the accounts and placing them in the machine. Ledger cards can be handled more rapidly than sheets on account of their greater weight and stiffness, whilst they are more resistant to the effects of frequent handling. The cards are usually placed in steel ledger trays each capable of holding about 1,000 cards with their guides. The trays are readily portable so that they may be stored in a strong room at night or in a special fire-proof file near the book-keeping machines.

**INSTALLATION OF MACHINERY.**—The volume of work entailed



in keeping the accounting records of a large business, coupled with the necessity for the rapid production of results, has led to the introduction of *mechanical methods* in this section of the business. The objects of mechanisation in the office are the same as in the factory, namely, to do work more quickly and at less cost. It follows, therefore, that unless the volume of work is sufficient to keep the machines continuously employed, they are likely to be less economical than the former methods. Hence, mechanical methods involving considerable capital outlay should not be introduced until the management is satisfied that some tangible advantage or economy will result. Again, the use of machinery in accounting requires somewhat different qualities from those engaged in the work than are required from ordinary ledger clerks. Steps should therefore be taken to ensure that the operators have had sufficient training before the machines are installed. In this connection most manufacturers are prepared to give assistance, not only in the training of an adequate number of machine operatives, but also in providing supervision for some time after installation. Again, it is necessary to avoid the mistake of over-elaboration of records, and the placing of work on the machines which is not essential to meet business requirements. Unless this point is kept in mind, it will be found that more machinery is being installed than is necessary, with the result that accounting and statistical expenses rise instead of decrease.

There is now on the market a very wide range of equipment for *mechanical accounting and calculating*, and the varying requirements of different businesses can be met by the installation of different systems. The following general considerations must, however, be kept in mind when arriving at a decision—

- (1) The speed and simplicity of operation.
- (2) The accuracy and the method of proof.
- (3) The capacity of being used for varying accounting operations.
- (4) Cost in relation to the advantages to be obtained.
- (5) Space required for efficient working.

As an example of the capabilities of these machines, the case of the National Ellis Accounting Machine may be cited. This is a combined typewriter, adding and listing, and book-keeping machine. The operator can type invoices, day book entries, ledger entries, statements, and, indeed, any form containing figures, and while



the work is being done the figures can be added or subtracted vertically or horizontally, or both. In using the machine for ledger posting, sheets or cards are placed in the machine, and the date, reference number, and description of entry, such as "To Goods," or "By Cash," are typewritten. While debit items are being posted the outstanding balance is being added, and the final balance produced. Each of these details is shown upon the ledger sheet. At the end of each posting period or at any intermediate time, the totals of all debit and credit entries can be obtained in a moment. These totals upon comparison with predetermined totals of invoices and credits, as shown by the day book, and credit and cash book, prove the accuracy of the operator's work, and form the basis of control accounts.

### TEST PAPER XVII

1. What are the functions of a modern office? Give a description of any modern office with which you are acquainted.
2. Why is the question of internal communication of great importance in planning an office system?
3. Explain the use of stenography in a modern office.
4. What are the advantages in the use of a typewriter?
5. Say what you know of the calculating machine.
6. Enumerate the most useful time-saving devices of the modern office.
7. How is a record kept of incoming correspondence? What is usually recorded?
8. Give some account of the different methods of filing.
9. Describe shortly the application of the Card Index System to the records in connection with any business with which you are acquainted.
10. State shortly the advantages of employing printed forms, with blank spaces to be filled up according to circumstances—
  - (a) For use between one department of a business and another;
  - (b) For use between a business and the outside world.
11. Describe a system of filing correspondence suitable to an ordinary business office.
12. A wholesale trading firm divides the area over which it trades into six districts, and is represented in each district by a commercial traveller. Suggest a suitable filing system for the whole of the firm's correspondence. Describe the basis upon which the correspondence would be split up for filing purposes, and how you would ensure that all papers were correctly filed?
13. For what purposes and under what circumstances should office machinery be employed? Outline the labour-saving devices you would employ for the following—
  - (a) Recording and acknowledging payments received.
  - (b) Issuing invoices for goods sold.
  - (c) Posting ledgers.
  - (d) Issuing monthly statements of account.
14. As the newly-appointed accountant to your firm, you have suggested to your directors that book-keeping machines be purchased. What advantages would you claim for the installation over their present system which may be supposed to be non-mechanical?



## CHAPTER XVIII

### AGENTS

WHEN commercial transactions embrace a more extended and larger sphere of operations, the clerical staff and assistants of the business are insufficient to cope with the work involved, so that it is usual to appoint agents such as brokers, commission agents, shipping agents, warehousemen, forwarding agents, etc. .

A **Mercantile Agent** means an agent having in the customary course of his business as such agent, authority—

- (a) To sell goods, or
- (b) To consign goods for the purpose of sale, or
- (c) To buy goods, or
- (d) To raise money on the security of goods.

Every person capable of contracting may appoint an agent to contract for him. It is not necessary that an agent should be capable of contracting in his or her own right in order to bind the principal—e.g., an infant or married woman. The nature and authority of an agent is defined in expressed terms, or implied from circumstances and conduct. Agents may be distinguished as

(1) **GENERAL AGENTS.** These consist of brokers, factors, commission agents, managers, etc., and all persons employed in business or filling positions of a general kind, the extent of authority being apparent from the nature of the positions.

(2) **PARTICULAR OR SPECIAL AGENTS.** These denote persons appointed for a special or particular appointment. A general agent has, in relation to third parties, full apparent authority due to his employment or position. The principal is bound by all his acts within the authority usually conferred, notwithstanding that—

- (a) the principal has never held him out as being his agent ; or
- (b) he has imposed special restrictive limits not known to the other party.

**FACTORS.**—A factor is a mercantile agent whose ordinary business is to sell goods with the possession or control of which he is entrusted by the principal. Hence a factor has implied authority—

- (1) To sell in his own name.



(2) To sell at such time and prices as he thinks best for the principal.

(3) To sell upon the usual terms of credit.

(4) To receive payment of the price and give a good discharge to the buyer.

Any private instructions restrictive of the apparent authority due to his character of factor do not affect his ordinary transactions unless they are unsatisfactory to the other contracting party. Under the common law a factor could not himself pledge the goods which came into his possession. But according to the Factors Act, 1889, where a mercantile agent, including a factor, is in possession of goods or documents of title, any sale, pledge, or other disposition of goods made by him when acting in the ordinary course of business will be as valid as if he were expressly authorised by the owner to make the same, providing he acts in good faith.

**BROKERS.**—A broker is an agent whose ordinary course of business is to negotiate and make contracts for the sale or purchase of goods. Hence a broker is primarily an agent to establish privity of contract between two parties, e.g. an intending seller and an intending buyer of goods. Where a broker is acting as an agent for sale, he differs from a factor in that—

(1) A factor is entrusted with the possession of the goods he is employed to sell, whereas a broker is not.

(2) A factor has authority to act in his own name and to sue in his own name on the contract made by him, whereas the broker has no such authority.

(3) A factor has authority to receive payments and to give a good discharge to the buyer for goods sold by him, whereas the broker has not.

(4) A factor has a lien on goods in his possession, whereas a broker in ordinary cases has not. But there are two exceptions—

A. **INSURANCE BROKERS** have a lien on all policies of insurance effected by them in their own names and for all premiums paid or payable by them to the underwriters with whom the policies are effected.

B. **STOCKBROKERS** have a lien on all moneys and securities of their customers which have come into their hands in the ordinary course of business for whatever balance may be due to them.

When a broker makes a contract he puts the terms of the contract



into writing and delivers to each party a copy signed by him. The copy delivered to the seller is called the sold note and the copy delivered to the buyer is called the bought note. The bought note is as follows—

## BOUGHT NOTE

1174

BANKERS · MIDLAND BANK, LIMITED, CARDIFF DOCK.

LIDGETT GIBBS &amp; CO.

(LIDGETT GIBBS)

STOCK &amp; SHARE BROKERS.

21, MOUNT STUART SQUARE,

AND STOCK EXCHANGE,

CARDIFF, 20th. September 19--.

**Bought**

by order and for account of

Mr John Weldon

Subject to the Rules and Regulations of the Stock Exchange.

£500. LONDON &amp; NORTH EASTERN RAILWAY COMPANY.,

4% 2nd. Preference Stock.

£163.

81 17 6d.

for Settlement 6th. October 19--.

Commission ..... 10 -

Transfer Stamp..... 1 - -

Registration Fee..... 2 6d.

Contract Stamp..... 6d.

83 10 6d.

E. &amp; O.E.

£

Please send by return enclosed form with full Name and Address in which the above is to be registered.  
When Buyers and Sellers are brought together, Brokerage is payable by both.

The sold note is usually made out as shown on page 211.

According to the scope of their operations, the following classes of brokers are to be distinguished—

A. PRODUCE BROKERS occupy themselves with the negotiation of the purchase and sale of goods, sometimes by the employment of a public auctioneer.

In many places, particularly in the large commercial centres and seaports, specialisation is carried to a very high degree, particular brokers being employed for each different class of produce. Thus there are tea, coffee, indigo, wool, yarn, timber brokers, etc.

B. STOCK AND SHARE BROKERS are concerned with the purchase and sale of Government securities, stocks and shares.

C. SHIPBROKERS are a class of agents who transact business



connected with ships, such as negotiating charters, procuring cargo, buying and selling ships, and filling up the necessary forms required for customs.

D. INSURANCE BROKERS are occupied chiefly with the negotiation

## SOLD NOTE

2969

BANKERS MIDLAND BANK, LIMITED, CARDIFF DOCKS.

LIDGETT GIBBS &amp; CO

(LIDGETT GIBBS)

STOCK &amp; SHARE BROKERS.

21, MOUNT STUART SQUARE,

AND STOCK EXCHANGE,

CARDIFF, 13th. December 19--.

Sold by order and for account of

Mr John Weldon

Subject to the Rules and Regulations of the Stock Exchange.

£500. LONDON &amp; NORTH EASTERN RAILWAY COMPANY.

4% 2nd. Preference Stock.

373

188 15 -

for Settlement 21st. December 19--.



Commission ... 1 - -

Contract Stamp ... 1 -

187 14 -

Member of the Cardiff Stock Exchange.

E &amp; O.E.

In order that Transfer may be correctly prepared please send Certificate or Scrip by return of post.  
When Buyers and Sellers are brought together, Brokerage is payable by both.

of marine insurance. They effect the insurance at Lloyd's or with an insurance company for and on behalf of the owner of the ship or of the cargo.

**COMMISSION AGENTS.**—A commission agent is a person employed, not to establish privity of contract between the employer and the third party, but to buy or sell goods for the employer on the best possible terms, receiving a commission for his exertions, e.g. where X, a merchant in Calcutta, agrees with Y, a commission agent in Manchester, that Y shall endeavour to procure a certain amount of calico, and when procured sell it to X, receiving not only the price at which the calico was bought, but a commission at, say, 5 per cent on the price as a reward for his exertions in procuring



the calico. The duty of a commission agent who is employed to buy goods for a principal is twofold—

(i) To procure the goods required by his principal as cheaply as possible

(ii) To charge the principal with the actual cost of the goods and the commission agreed upon and nothing more.

Hence if he charges his principal either directly or indirectly a higher price than he has himself paid for the goods it is a fraud on his principal and the principal can compel him to account for all secret profits made by him in connection with the transaction.

The commission agent engaged in the foreign trade acts in his own name, but for the account of either the foreign buyer or importer or on behalf of the home manufacturer. He must have a special knowledge of the goods in which he deals ; and must keep in close touch with the movements of their prices and with any alterations which take place in the process of their production. The primary object of the commission agent is to obtain orders from foreign buyers and then to pass them on in his own name to the home manufacturers. Moreover he has to supervise the execution of these orders and bring them to a satisfactory conclusion. In his dealings with the manufacturer, the commission agent acts in the interests of his principal, and insists on the goods being made according to sample, and on the delivery being effected by the date arranged. He also undertakes the work connected with the dispatch of the goods, such as the arrangements with the shipowner, the preparation of the bills of lading, the procuring of the Customs documents and the effecting of the insurance.

A *DEL CREDERE* AGENT is employed to sell the goods of his principal and, in consideration of a higher remuneration than is usually paid to agents, gives an undertaking to his principal that the parties with whom he is brought into contractual relations will perform the engagement into which they enter. In some trades a *del credere* commission is annexed to the employment of the agent by the usage of the trade, and therefore the contract need not be in writing.

**FORWARDING AGENTS** are persons employed to collect and deliver goods on behalf of others.

The merchant usually utilises the services of the forwarding agent in the dispatch of his goods. This is necessary especially



in the consignment of goods across the sea, as the shipping companies do not hold themselves responsible for the conveyance of goods from the railway to the quay. The forwarding agent is also indispensable to the home trader who is in receipt of his supplies from abroad. It is his duty to be at the port of importation to receive delivery of the goods and to examine their quantity and quality, and to attend to either their warehousing or their onward transmission. Apart from these circumstances, it is almost always advantageous to the merchant to engage the services of the forwarding agent, because—

(1) The forwarding agent can forward separate parcels cheaper than the railway. He collects the various packages addressed to the same town or district from the different consignors into one consignment, and is thus enabled to avail himself of lower rates.

(2) Special privileges are usually granted by railway companies to forwarding agents so that it is often more economical for the public to deal with the latter than directly with the railway companies.

**UNDERWRITERS** are persons who, in return for a certain commission, undertake that if the public do not take up shares in a company that is being floated, they themselves will take up and pay for a certain number of the shares. They are appointed by the company promoter. According to the Companies Act, 1929, a company may lawfully pay a commission to an underwriter in consideration of his subscribing or agreeing to subscribe whether absolutely or conditionally for any shares in the company provided—

(a) The proposed payment does not exceed the amount or rate authorised by the Articles of Association or 10% of the price at which the shares are issued, whichever is the less ; and

(b) The payment and its amount or rate is disclosed in the prospectus or in the statement in lieu of prospectus.

**AUCTIONEERS** are agents for both the buyer and the seller, although it is the seller who usually pays their commission. Where an auctioneer advertises a sale by auction “without reserve” he has implied authority and is indeed bound to sell to the highest bidder. Being an agent of both parties, he is empowered to make the necessary signed memorandum on behalf of either party which is required by the provisions of the Sale of Goods Act, 1893. Where



he is in possession of the goods for the purposes of their sale by auction, he has a lien upon them for his charges.

**MANUFACTURERS' AGENT.**—This type of agent is one who represents a number of manufacturers in a particular district. As a rule, he is given an exclusive agency for his area. He carries on business on his own account and on a commission basis.

**WAREHOUSERS** are persons acting in the capacity of agents, whose business it is to receive goods for the purpose of storage, for which they make a charge.

Warehousing consists in putting commodities in a place of safe keeping until such a time as the market or the consumer can use them. Storage has always been recognised as a fundamental economic service in the smoothing out of supplies, the object being to adjust supplies to the buyer's needs so that price levels are kept steady and even.

A warehouseman is bound to exercise reasonable diligence in preserving the goods, and has a lien on the goods until his charges are paid, i.e. he can retain the goods until he receives payment for warehousing them.

### TEST PAPER XVIII

1. What is a Mercantile Agent?
2. What are the different classes of agents?
3. Distinguish a factor from a broker.
4. Enumerate the different kinds of brokers, and explain the function of each.
5. State clearly the duties of a Commission Agent.
6. What is a "Del Credere" commission? Explain what benefit accrues to the merchant through its payment.
7. Why do merchants engage forwarding agents to collect or deliver their goods?
8. Under what conditions may a company pay a commission to an underwriter?
9. For which party does an auctioneer act as agent, and who pays his commission?
10. What classes of persons are entitled to a *lien* on goods in their possession?
11. George Brown, 27 Wine Street, Bristol, asked his broker, Walter White, The Exchange, Bristol, to buy 100 Vickers Ordinary shares. He does so and sends him a Bought Note containing the following details: 100 Vickers Ordinary shares at 7s., £35; commission, £1; stamps, £1 1s.; registration fee, 2s. 6d. Draw up the Bought Note.



## CHAPTER XIX

### METHODS OF REMUNERATION

REMUNERATION usually takes the form of a monetary payment in consideration of services rendered, but it must not be overlooked that the monetary consideration in itself is of little use to anyone, and that the real benefit received by the worker employed is represented by the purchasing power of the money received. From his point of view, therefore, fluctuations in the purchasing power of money will materially affect the problem as to whether he is or is not satisfied with an existing bargain. From the point of view of both employer and employee, it would be unwise to look too closely to immediate results and to neglect ultimate results. Unfortunately, however, the employer is usually in a position to take a long period view, whilst the employee is not.

The main thing the employer requires to provide for in taking a long period view is a continuous supply in sufficient numbers of those possessed of the kinds of abilities he requires for his purposes, and in so far as it may be necessary for him to train his staff so that they are especially suitable for these purposes, he is obliged to take a long view so as to make sure that he will have the necessary supply of workers in the future, as well as in the present. The employee, on the other hand, wants continuous employment of a kind suitable to his talents ; but, together with that, he usually requires increasing rates of remuneration, because his wants have a very natural tendency to increase. This particularly applies to an employee who is comparatively young. There are only two ways in which a worker may expect to receive an increasing income—

(1) By a contract under which less than the fair rate is paid in the earlier years in consideration of increased payments later on.

(2) By the worker improving his efficiency and thus being able to increase his output or undertake more responsible work.

**ESSENTIALS OF A WAGE SYSTEM.**—The first essential towards a solution of the wages problem is to devise a method of payment which will meet with the approval of workers and employers. The chief requirements are—

(1) The employer must have an adequate return for his



expenditure, so that work must be done within a reasonable time, and must be of good quality.

(2) The minimum rate must have some relation to the cost of living in order to ensure a "living wage."

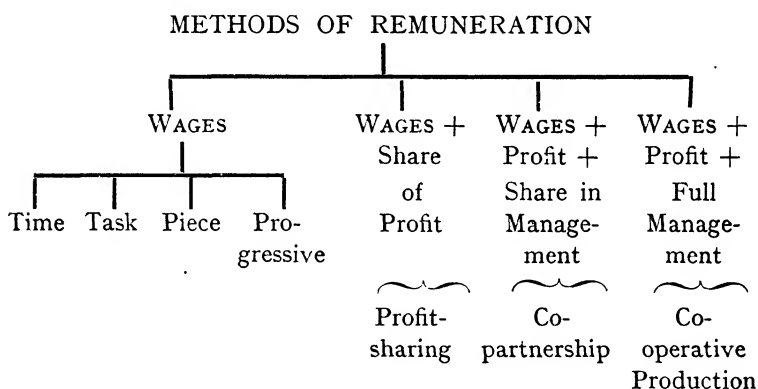
(3) The system of payment should be easily understood even by uneducated employees.

(4) Any rate, when once fixed, should not be altered without good cause.

(5) Wages must be adjusted equitably to meet changing conditions.

**SYSTEMS OF PAYMENT.**—Many different systems exist for the payment of wages, but those best known are Time, Piece, Task, and Progressive Wages. There are, of course, a great many modifications and combinations of these:

These systems will now be dealt with in the order shown in the following diagram—



**TIME WAGES.**—A time wage is the amount of conveniences and necessities of life that a man obtains in exchange for a given *period* of his labour. In England the payment takes the form of a fixed sum of money per hour, day, week, month or year for the performance of a certain kind of work. The system of time wages is the one most in vogue in this country, owing to its many advantages. With regard to this system, the following may be stated—

(1) It is the most suitable, and is preferred by the employer and the employed where quality of work is of the highest importance and where quantity is of smaller consideration.

(2) Where the product is the result of a number of different



operations, performed by different hands, it is difficult to assign a value to the share of work performed by any particular individual, and, therefore, time wages are usually adopted in such cases.

(3) Time wages are in favour where delicate machinery, which must not be subject to rough usage, is in use.

(4) Sometimes work has to be set by one worker for another ; hence it would be unfair to pay the latter according to quantity of work done, since the amount he can do is regulated by another person.

**TASK WAGES.**—In the case of task wages, the labourer is paid according to the period of time he is engaged, but on condition that he does not turn out less than a certain amount of work during that period. If he is paid a certain weekly wage, he must complete a minimum amount of work. If he does more than this minimum he receives no extra remuneration. Naturally, task wages are disliked by workmen. They must be distinguished from piece wages.

**PIECE WAGES.**—These are payments of certain sums of money for the piece of work completed, or brought to a certain stage, without regard to the time occupied. The system of piece wages is not only preferred but is insisted upon in some districts where trade unions are very powerful. Other unions strongly object to the system and will not allow their members to accept it.

Of course, under a system of piece wages, quality need not be sacrificed to quantity, for that is purely a matter of adequate superintendence and inspection. As a rule, however, piece work does lead to more work being turned out in the time. This system of payment is in favour among a certain section of workers because it ensures that each unit of labour shall get its due reward. Hence the tendency to "screwing up" by the employer is checked.

Again, according to regulations, which are very easily made, piece work admits of consideration of the quality of the machinery placed at the disposal of the worker. In factories, the standardised wage takes into consideration the quality of the machinery.

In piece work a man is paid a certain rate per unit of work done, but when he is called upon to work with imperfect machinery, he cannot in the time produce the same quantity, so that the trade unions arrange that he shall be allowed more per unit of work.

Sometimes, however, the workers object to piece rates, particularly in the case of sub-contract work. Here the workmen are divided into groups, at the head of each being a foreman, who



receives all the money and then pays out the piece wages to the men, keeping the rest for himself.

The chief disadvantages in connection with piece work are—

*Moral.* There is a temptation for the operative to rush his work during the first few days of the week, and then idle about.

*Hygienic.* Over-pressure may lead to a deterioration in the health and physique of the operatives, although the effects vary with different industries.

*Economic.* The adoption of piece rates may lead to the scamping of work. Very high speed is often detested by the best workmen because they take a pride in their work and prefer to finish it off properly. They dislike the prevailing motto of the piece work system, viz. "near enough."

An objection, which is quite fallacious, i.e. the lump of labour fallacy, is sometimes made to piece work. According to this theory, piece work leads to one man doing more, and, in consequence leaving less to be done for other men, and thus causing unemployment. The shortest answer to this is that the argument proves too much. If unemployment is diminished by arranging for men to do less work, then it should be abolished altogether by arranging for them to do nothing.

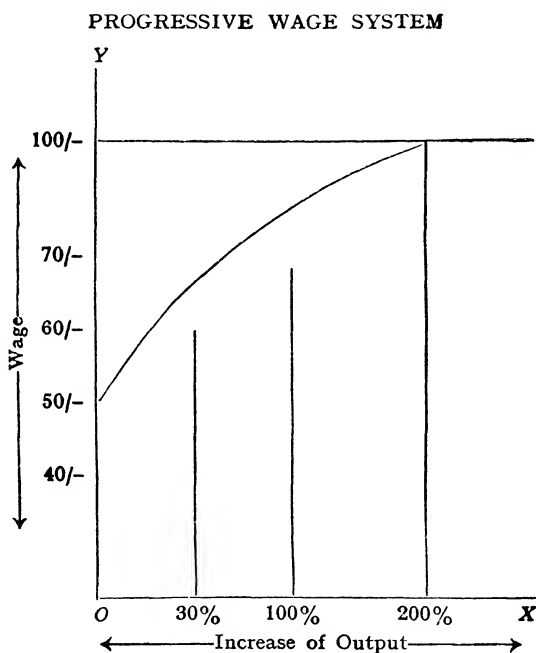
As a matter of fact, this lump of labour fallacy is founded on a misconception of the construction of society. The idea underlying it is that there is a certain amount of work which must be done, and that this is divided out among a certain number of men. This is fallacious, however, for there is no definite quantity of work divided out among the men. Take any article, e.g. a box of steel pens. A certain number of boxes of steel pens will be sold in a year, but only on condition that they are sold at a certain price. Directly a measure is taken to raise their price, the demand for the steel pens will fall. The community will purchase a smaller number of boxes at the increased price. Hence the amount of work to be done is not stationary, but will be determined by the price of the commodity.

**PROGRESSIVE WAGES.**—In this case there is a fixed minimum time or piece wage supplemented with a premium for extra efficiency; that is, an increase of pay is given on an output above a certain amount, and a further increase on a still greater output. For instance, a wage of 50s. per week may be offered, together with five shilling extra if the quantity produced exceeds a certain amount.



In a progressive system of wages, a man would get a certain piece rate up to a certain output, but beyond that output he would get a lower piece rate for additional quantities. The idea is to encourage briskness and at the same time to discourage rushing. If a worker can easily increase his output, it will pay him to do so, but the reward is not so great as to encourage him to increase his output beyond a certain point. However, if he is an exceptional workman, he is enabled to benefit by his extra efficiency.

Take, for example, the case shown in the following diagram—



Suppose the wage of the normal man is 50s., and that unless a person can earn this amount he is no longer employed. With regard to the exceptional workman his wage is permitted to increase up to a certain limit, which is continuously approached by increased speeds, but is never reached. In the diagram the limit is fixed at 100s., and an increase of 30 per cent. on the normal output will result in a wage of 60s., and 100 per cent. increase in that of 70s. Thus under this system scope is given for extraordinary efficiency,



although a check is placed in some degree on the expansion of the output per head at the expense of the quality of the product.

**Gain Share.** One of the best known forms of the progressive wage is the Gain Share. Here the plan is for a standard time to be set for the performance of a certain amount of work, and then a premium is offered for every hour the workman can save in its execution. This is applicable in cases where large quantities of an article are turned out, the production of which involves the repetition of the same operations ; for instance, the production of a nut for a certain part of a bicycle. Suppose a gross is normally turned out by a man in a week ; then if he finishes his job before the stipulated time has expired, there is a saving, of which he will receive a share. This must be distinguished from actual profit-sharing.

**PROFIT-SHARING.**—This does not occur unless there is a definite contract made, between employers and employed, which is enforceable at law. In addition to the worker's salary, a fixed bonus in proportion to the net profits of the firm is usually given. In those occupations in which piece wages are difficult to arrange, time wages have often been found to necessitate a great deal of supervision. Hence, systems of profit-sharing have been devised to give employees an interest in the success of the undertaking.

Although individual schemes of profit-sharing may differ more or less in detail, they all contain this central idea—that in the long run it will pay the employer or those having a proprietary interest in a business to concede some share of the profits of the business to those who are engaged in it, over and above whatever they may be paid as wages for work done.

The arguments advanced in favour of profit-sharing are that as soon as one can get the employees financially interested in profits, they will also take a real interest in the business, so that they will become more careful in the use of materials and less wasteful in regard to time. It will, therefore, be possible to economise in the matter of superintendence, since the men will require less watching, and to some extent will keep a watchful eye upon each other. In consequence the work turned out will be improved, and its value enhanced. Finally, these factors will tend greatly to reduce the risk of industrial disputes, strikes, or lock-outs, and the men being interested in the profits of successful management will be more ready to aid management with suggestions as to improved methods.



The underlying idea is that if the workers are given an active interest in the business, they become more efficient, so that the net result is an increase of production, a smaller amount of waste, and a greater return to each factor in production.

**CO-PARTNERSHIP.**—Profit-sharing is distinguished from labour co-partnership in that it does not involve sharing in the control of the undertaking. Co-partnership is an attempt to give to labour a share not only in the profit of industry, but in its responsibilities also, in the belief that successful enterprise depends on the hearty co-operation of all those engaged in it.

There is, it is true, great diversity between existing co-partnership concerns. At one extreme are such undertakings as the boot manufacturers at Kettering, whose system almost resembles productive co-operation, differing only in the fact that they have capitalists on the board of directors who do not work in the factory. In fact, the system may be described as productive co-operation leavened by capitalistic advice.

At the other end there are cases which are barely separated from profit-sharing. Here the operatives exercise but little control, the chief function of their representatives being to voice grievances.

Complete co-partnership involves—

- (1) The payment of the existing standard wages of labour.
- (2) The payment of a fixed rate of interest on capital.
- (3) The division of the surplus profit between capital and labour in agreed proportions.
- (4) The payment for part of the workman's labour by the allotment of shares in the capital.
- (5) A sharing in the control of the business by the representatives appointed by labour.

Co-partnership is a recognition of the claims of the dignity of labour, while preserving the rights of capital.

**PRODUCTIVE CO-OPERATION.**—This is an attempt to avoid the antagonism between capital and labour by giving to the labourer the profits which accrue to the possessor of capital. In such enterprises the labourers own the capital, the employer is eliminated, and the work of organisation is undertaken by an elected representative. This form of co-operation has made little progress in England as compared with co-operative distribution.

**SCIENTIFIC MANAGEMENT.**—In the main this is a method of



redistributing and reorganising the functions and the mutual relations of the staff of a large business, with the purpose of increasing aggregate efficiency, by narrowing the range of responsibility of most of its employees. It approaches the problem of remuneration with a view to the determination of a standard rate of wages. Time wages give no direct stimulus towards efficiency, and piece-rate wages have no relation to the cost of running plant. The aim of scientific management is to ascertain the time which a job requires when performed with standard provision of accessories, and by a workman of fair average ability. It sets a standard wage which corresponds to that standard time, and finally it increases the wage for the whole of the job for every diminution below the standard of the time which the workman detains his plant on it. It claims that very high efficiency of plant can be obtained without overstraining the operative in charge of it, by supplying him with high standard conditions of work, and causing his remuneration for each job to increase with every increase in the speed of its performance.

### TEST PAPER XIX

1. What effect have fluctuations in the purchasing power of money upon the relations between the employer and the employed?

2. In what two ways may a worker expect to receive an increasing income?

3. Mention the chief systems in existence for the payment of wages.

4. Compare and contrast "Time," "Task," and "Piece" Wages.

5. Discuss the advantages and disadvantages of a system of paying wages to workmen at rates varying with the speed of the work. Give examples in connection with any industry with which you are acquainted.

6. State three different methods of remunerating workmen at rates varying according to the speed with which their work is executed, and discuss their relative advantages and disadvantages—

(a) as compared with each other;

(b) as compared with a fixed rate per hour.

7. What do you understand by profit-sharing and co-partnership? State the aims in each case and note any advantages that accrue from each and any difficulties that may stand in the way.

8. Enumerate the different methods of remuneration existing in modern British industry. Is there any connection between the "method" and the "amount" of remuneration?

9. State, with reasons and in order of merit, the types of wage payment by results most suitable for a factory turning out a uniform product of one size.

10. Discuss the possibilities of promoting general happiness among industrial workers by Act of Parliament, and illustrate your remarks with examples of what the modern employer is doing for his workers.



## CHAPTER XX

### GOODWILL OF A BUSINESS

As a question of law, goodwill is recognised as the right to represent oneself as the successor to an established business. As a rule, it carries with it the right to use the trade name and also any trade marks that may have been employed in that business beforehand. The law regards goodwill as property which is transferable, and the rights acquired by a purchaser are accordingly enforceable in so far as they have been enforced by an agreement to transfer. The agreement to transfer usually contains a covenant that the vendor will not carry on a competing business within a given area or within a given time. Even if there is no such stipulation, the fact that a man has sold his goodwill to another is held to preclude him from canvassing former customers.

If a person or a company starts an entirely new business which has to be built up, its equipment put together and its organisation worked out, then, during the first few months, one cannot expect anything like such satisfactory profits as may be looked for later on, when the business is in proper working order, and it has acquired a certain reputation with the public. As a rule, a successful business has a satisfactory reputation with its customers unless it is a monopoly. With a monopoly there may be large profits without satisfying anybody, but so long as free competition prevails, the successful business will be the one appreciated by the public. The result is, that an established business, and particularly one with a good reputation, can naturally expect to make better profits than one which is absolutely in its infancy. This suggests that any concern which has overcome the initial stage of building up its reputation is in a better position than any new-comer which has to start from the beginning, even if the new-comer has advantages with regard to newer machinery, buildings, etc. The old business will hold its own until the new firm has established a reputation for good work.

Hence, it may be said that *goodwill is that intangible something which one associates with the reputation for conducting a business in a manner satisfactory to the customers.* It requires considerable



energy, experience, and often the expenditure of much money in experimenting and advertising, before such a reputation is established.

If it is desired to sell the business after having rendered it into a profitable concern with a good reputation, payment may be expected not only for the assets at the figures which appear in the accounts, provided they are reasonable, but also something over and above that amount for what is called the goodwill of the business ; and the reason why people are prepared to pay for the goodwill of the business is because its acquisition places them in a position to earn larger profits than if they had to start a new business.

The price paid for the goodwill will depend chiefly upon the eagerness displayed by intending purchasers. A person very confident that he could establish a similar business in a few weeks, would be less willing to pay a high price for the goodwill than another person with little energy and hope. In each case, if there is any real value in the goodwill it is because a purchaser may expect a distinct advantage from buying the business rather than attempting to build up a new one.

The question of goodwill centres round one or more of three things—

(1) **The Name.** Goodwill is closely connected with the name of the business. In the case of a bank, the name is almost everything.

(2) **The Situation.** The actual situation of the business is, in many cases, more important than the matter of the name. A particular situation may be found to be very suitable for a particular class of trade, as in the case of a large hotel where proximity to a railway station is important.

In the case of a theatre, the situation is often more important than the name. If the theatre is removed from one place to another, although the name may be retained, it does not follow that the same number of persons will continue to patronise it. The same thing applies to shops. The goodwill of an ordinary retail shop is largely due to its situation, and so long as there is a draper's or a grocer's shop at the corner of a particular street, the people will continue to make their purchases at that place.

(3) **The Trade Mark.** Perhaps an even more stable form of goodwill than the name or address is the trade mark which is



associated with the kind of goods desired by the people. Here the manufacturer gets into contact with the people because they know his goods. In this case, there is less risk that the goodwill will not be transferred, since it is the goods that are known and not the trader.

There will, of course, always be some part of goodwill which cannot be transferred, such as part of a medical practice which is due to the personality of the doctor. All that can be conveyed to the new-comer is the right to regard the patients as his customers. The patients may have such faith in the doctor that they may take his word as to the skill of his successor. But the goodwill of a medical man cannot be transferred like that of an ordinary commercial business. The same holds with regard to an actress, violinist, or other calling based on personal skill.

If there be such a thing as a transferable goodwill, it must be possible to arrive at its price, and goodwill must come into the accounts as an asset. It will not be brought into the accounts while it is being built up, however, for its value is too uncertain to record.

If the business is being carried on with increasing profits, then it is reasonable to argue that the value of the goodwill is increasing, although it would be difficult to record the amount of the goodwill. It would be impossible to assess on a satisfactory basis the increase in value from year to year, and when it had been done the result would be useless.

Suppose the goodwill of a business had, in fact, increased by £1,000, it would not enable us to draw out a similar amount from the business, because there would be no addition to the amount of money. The practical effect would be that it would reduce the working capital by £1,000, thereby resulting in a decreased efficiency to that extent, which would soon decrease the value of the goodwill. There is, therefore, no practical benefit derived from periodically assessing goodwill; in fact, this should be done only when the business is about to change hands.

With regard to privately-owned businesses, the need for valuing goodwill does arise when one of the partners dies and there is a sale of the business as a whole, or when there is a sale of part of the business, as when one partner retires and the continuing partners buy out his share. The place of the retiring partner may be taken by a new incoming partner, or there may be a new incoming partner



without anyone retiring, in which case the additional partner acquires a share of the goodwill of the older partners. The goodwill being in reality the asset which represents the right to the future profits of the business, it will, in all cases, belong to the partners in the same ratio as they share profits unless there is a provision to the contrary.

Goodwill is, *prima facie*, an asset which must be realised along with the other assets when the business is being sold. By a special arrangement, however, it is quite possible for a partnership agreement to provide that the goodwill belongs to the senior partner, and then, in the event of a dissolution the junior partners would be entitled to receive nothing in respect of goodwill, and the senior partner could continue the business.

The necessity arises, therefore, to find out the value of the goodwill of a business whenever the whole or part thereof is changing hands. Inasmuch as the goodwill is really the right to carry on the business and to receive its profits in the future, it is clear that the real value of the goodwill fluctuates as continuously as the profits themselves. When the necessity does arise to ascertain the value of the goodwill, it represents the price the vendor is willing to sell it for and the price at which the purchaser is willing to buy it. It would be necessary to show goodwill if we were making a statement of our wealth, but otherwise there is no need to value it.

On the death of a person, the property passes from the deceased to his executors or administrators, and duty has to be paid on his assets, including goodwill. Therefore, at death it becomes necessary to value goodwill to see what estate duties have to be paid. This is the only time when goodwill has to be valued except for the purposes of sale. On these occasions, the Commissioners of Inland Revenue are the final valuers of all property for the purposes of duty. There are no definite rules laid down, but the goodwill would be valued by them at decidedly less than its realisable value. In the matter of valuation, the Commissioners reserve a perfect freedom of action. But when it becomes a question of valuing the goodwill for the purpose of arriving at a deal between purchaser and vendor, then the matter is one of negotiation between the parties.

In many cases, however, the parties are willing to abide by the decision of a valuer, so that it is worth considering how it is valued at the time of sale.



**METHOD OF VALUATION.**—There is a common idea that the goodwill of a business is worth three years' purchase, that is, the actual amount of the profits earned during the past three years. Like many other popular ideas, there is not much foundation for this in practice. The goodwill is worth what it will fetch and nothing more. It would be manifestly unreasonable to apply the same principles to all kinds of businesses. To begin with, if the value is to be based on the profits of the last three years, it is quite possible for the same profits to be earned in two concerns, but in one there has been an increasing profit, whilst in the other there has been a falling off in the profits.

For instance, in one business, say A, the actual profits for the past three years may be £700, £600, and £500; whilst in B they are £500, £600, and £700. No one would say that these two businesses were equally valuable because they have earned the same amount of profit during the past three years. The real estimate is on future profits, and the price should be based on what the vendor and the buyer think the future profits are likely to be; but since they do not know what the future profits will be, they have to assess on the basis of past profits. Hence, one only uses past profits because the future profits are not available for the purpose.

In the case of B, it may be argued that the profits next year are more likely to be £800, whilst in the case of A they are more likely to be £400, so that on this basis the probability is that the goodwill of the first is worth twice as much as the second.

It must also be remembered that in every kind of trade or occupation there are good years and bad years, quite irrespective of the fortunes of the particular business. There are years in which businesses will make good profits and years in which they will make small profits, and these periods of adversity and prosperity seem to come in cycles. There is a vast difference between the profits one may expect to earn in good times and those earned in bad times. Suppose in the case of B mentioned above, the highest point of the cycle had been reached, it is quite likely that the profit for the following year will reach only £600, whereas in the case of A the lowest point of the cycle might have been reached, and the profit next year would be greater.

In some concerns it will never pay to work at a loss, whereas in others a loss may be expected and withstood every fifth year or



so. Hence, a much broader view of profits must be taken if a fair estimate of good will is to be obtained.

Moreover, other things being equal, the smaller the amount of capital that is invested to produce a profit, the more valuable will be the goodwill. Whatever capital has to be put into a business is ventured and is liable to loss. One business may work with £2,000, another with £10,000 capital, and both make the same profits. The usual plan is to charge interest at 5 per cent per annum on capital, and then consider the amount of profits as that remaining after the deduction of interest on capital, remembering that calculations of goodwill are based on profits. Further, the business which can be run profitably with the least management has the greatest amount of goodwill.

**Analysis of Profits.** The net profit which emerges from the trader's Profit and Loss Account is frequently capable of further analysis. It often happens, especially in a small business, that the trader has made no allowance for a management salary for himself, nor for a return by way of interest on his capital investment. If allowance were made for these matters at a suitable rate, the residue would consist of what the economist terms *pure profit*. This concept is designated by the accountant as *super-profit*, and the goodwill of a business may be expressed as so many years' purchase of this super-profit. This method is by no means free from difficulty since the allowance made for interest and salary must be very arbitrary in character.

Wherever reliable accounts are kept, there is no surer basis for the calculation of goodwill than by considering the net profits for a period of years. In doing so, it must be remembered that it does not necessarily follow because certain profits have been earned in the past that, in consequence, they will be earned in the future. The probability of their being earned in the future depends upon the conditions remaining the same, and on the transferability of the goodwill so as to allow the purchaser to carry on the business as satisfactorily as the vendor has done in the past.

In some cases a more rough and ready method has to be employed in the calculation of the value of goodwill, owing to the fact that no reliable accounts have been kept to show the past profits of the business. The practice has, therefore, grown up in many trades of assessing goodwill on the total sales for the year, as in the case



of a draper's or grocer's shop. Sometimes the total sales in money, and at other times the quantities handled are taken as the basis.

In dairies the practice is to base the goodwill on the quantities of milk sold, and in the case of public-houses on the quantities of intoxicants.

These are very rough and imperfect standards, because in each case they never represent the whole of the business, for a dairy sells other things besides milk. This method of choosing the essential commodity as the basis for the valuation of goodwill often leads to fraud, e.g. fictitious customers have been served regularly so as to increase the output and thus inflate the magnitude of the business.

The goodwill having been purchased at a given price, it must now appear in the Balance Sheet of the firm as an asset. It is money invested with a view to assisting in the earning of future profits. Whatever, therefore, has been actually paid for the goodwill of a business may be regarded as capital expenditure, since it is money expended in acquiring a fixed asset.

### TEST PAPER XX

1. What is the meaning of "goodwill" ?
2. Trace the origin of "goodwill."
3. "The question of goodwill centres round one or more of three things." Criticise this statement, and name the three things referred to.
4. In what way does the location of a business influence "goodwill" ?
5. Why is it necessary to estimate the value of "goodwill" on the retirement of a partner in a firm ?
6. Enumerate the circumstances under which goodwill should be valued.
7. "The goodwill of a business is worth three years' purchase." Criticise the truth of this statement.
8. What factors should be taken into account in the valuation of goodwill ?
9. Give an analysis of profits; and bring out the main points of resemblance and difference between earnings of management and ordinary wages.
10. When should the value of goodwill be shown in the Balance Sheet ?
11. Show the connection between goodwill and profits.
12. The goodwill of a business may arise in different ways, according to the nature of the business. Give two examples with the special feature in each that might make goodwill valuable, and one example where goodwill would be non-existent. How generally is the value of goodwill calculated ?
13. Assuming that you are a prospective buyer of a retail business, advertised as a "going concern," what inquiries would you make prior to actual negotiations, and how would you arrive at an estimate of the valuation ?
14. In disposing of a retail business, what would you stress when taking goodwill into consideration ?



## CHAPTER XXI

### ADVERTISING

THE original meaning of the term "advertising" was not so much to "draw attention" to things as to "turn persons away" from them—an advertisement is therefore primarily a warning. Even in connection with modern advertisements they are sometimes expressed in the form of a warning against imitations, substitutes, or against infringement of patents, etc. But advertisements have certainly departed widely from this original idea of warning the public and are now chiefly devoted towards attracting the public.

**CLASSES OF ADVERTISEMENTS.**—Advertisements may be divided roughly into two classes—

- (1) Advertisements of *Sales* ;
- (2) Advertisements of *Wants*.

The advertisements of sales are certainly those on which most money is spent and therefore those most usually seen by the public.

But there are also advertisements of wants, and on the whole the possibilities of advertising in this connection do not seem to be nearly so well developed as those of sales, supplies, or offers. The vast majority of the advertisements for wants are in connection with "situations" and with "houses."

Apart from "Situations Wanted" and "Houses Wanted," the next class of advertisements of wants is practically limited to cases in which the law requires that wants shall be advertised. Public bodies, for instance, have to invite tenders for the different supplies they require. If the idea is a good one in connection with public bodies, the possibility of applying it to ordinary business concerns is worth considering. It is argued that if a public authority is subject to competition it will buy at a better price and there will be greater efficiency in buying, as well as a smaller amount of corruption.

The force of this argument is diminished for two reasons—

(1) Great publicity in the requirements of exceptional quantities of a particular commodity tends at once to raise its price. This is



the strongest argument against advertising wants at all. The publication of the wants naturally creates an artificial scarcity which tends to force up prices.

(2) Competition is useful only to a certain degree. If the position is such that it would pay competitors to combine, then they will be quite ready to do so when it suits their particular interests. Even in the case of a local authority advertising for tenders for comparatively small quantities of goods, it is generally found that those business concerns that might naturally be expected to reply have come to an understanding among themselves. Matters are so arranged that they take it in turns to quote the lowest prices, and then pool the profits afterwards.

It may be argued that if a business man advertises his wants he would be placed at a disadvantage in bargaining. However, the mere advertisement of wants need not necessarily refer to present wants, and the business man should always buy in advance of actual requirements.

**ADVERTISEMENTS OFFERING GOODS OR SERVICES.**—Many persons, anxious to increase the volume of their trade, look to advertisements for assistance. The success of advertising depends upon its aim. It may have reference to an undertaking of a temporary nature or to a business which is expected to yield permanent profits. In the latter case advertising may be regarded as coming under two distinct headings—

(1) That which will have to be continued year after year, and which represents a permanent expense, just as much as packing materials or carriage. That is, it is an expense without which the sales would invariably decline.

(2) The preliminary expense of advertising with the object of making the article known. This initial expense is usually very heavy.

If the commodity which it is proposed to advertise is incapable of being developed into a permanent business on profit-earning lines, the preliminary expenditure on advertising will be wasted ; since, if it is to be effective, it will more than swallow up the profits. If a commodity is really worthless, this will soon be discovered, and any kind of advertising will be useless. The real function of an advertisement is, therefore, to draw attention to a really good commodity.



Although much money is wasted on advertising, it is none the less an important factor in connection with most business concerns which are successful. It will therefore be necessary to examine how advertising can be used.

**ADVERTISING POLICY.**—Assuming that the commodity is worth advertising and that there is every reason to believe that it will eventually prove a profit-earning article, the advertisement may be put forward in different forms—

(1) **EDUCATIONAL.** This policy aims at explaining the uses of the commodity to be advertised, which are not at present understood. This may be developed into persuading people that they have need of something without which it is impossible to manage. Its aim is to create in the mind of the person who reads the advertisement the feeling that he has missed something all his life which can now be readily supplied.

(2) **PUBLICITY.** This does not deal with explanations but simply aims at publicity. It states a few words to the public and leaves the words a mystery. Its object is to incite curiosity in the people who read the advertisement. The key-note is simply “publicity” —trusting to the curiosity of the public to follow it up. Sometimes this policy is successful, although it is well to supplement it with the educational policy.

(3) **INDIRECT APPEAL.** Another form of advertisement which is found to be very useful is an appeal, not to those who are going to spend their money, but to those who may be able to influence such persons in making their purchases.

Examples of this are to be found in connection with advertisements which offer handsome presents in exchange for coupons granted with each unit of the commodity sold. The object of this form of advertisement is to appeal, not to the public as a whole, but to a section of the public, such as the housewife of the smaller household and the domestic servant of the larger household. In each case an attempt is made to quicken their imagination by placing before them a scheme whereby they can get something for nothing. This form of advertisement is not very expensive.

(4) **ENLISTING NEWSPAPER SUPPORT.** This is a form of advertising which is resorted to particularly in the case of issues of capital in connection with new companies.

(5) **EDITORIAL ADVERTISEMENTS.** A form of advertisement which



has come very much to the front of late years, is that which is so arranged as to look like editorial comment or original matter in the daily newspaper. Whole columns are often devoted to chatty matter concerning the goods on sale in different shops or the unique bargains which are being offered at certain spring sales. Sometimes weekly articles appear on the subject as to how men should dress, or as to the various outfits for ladies. So long as one can be reconciled to doing business on these lines, that form of advertisement is probably much more effective than those in the ordinary advertisement columns, since it is much more likely to be read.

(6) CREATING A SCARE. Some firms are in the unfortunate position that their staple commodity is one which is not always in demand, e.g. cartridges. In order to encourage sales, something in the nature of a war scare may be inserted in the papers. This is, no doubt, a thing which has to be done with great discretion, although it has certainly been done in more than one country. It is argued, and perhaps rightly, that these should not appear as editorial articles unless the editor is willing to admit that they correspond with his own views.

**METHODS OF APPEAL.**—Having decided what kind of advertising policy should be adopted, the next step is to draw up a suitable appeal. There are various methods of doing this, some of which are as follows—

(1) CIRCULARS. The distribution of circulars by hand or through the post is one of the earliest methods. Upon the whole, however, circulars are probably the most ineffective form of advertisement, since the great majority are never read. The only kind of any use are those which are so short that they can be read at a glance.

(2) NEWSPAPER ADVERTISEMENTS. These are, of course, a favourite form of advertising. Here the disadvantage is that the cost of a newspaper advertisement is heavy owing to the number of advertisements contained in the newspaper, and the majority of advertisers have to be content with little space. If one could ensure the whole of the advertising space of the issue, it would be a good speculation, although an expensive one.

(3) MAGAZINES. One great advantage of the magazine over the weekly or daily paper is that it continues in use over a period of time. The magazine is kept for several weeks, and each separate copy is probably seen by a large number of different persons. The



advertising columns of a magazine are read to a greater extent than those of the average newspaper and, therefore, there is a good demand for such space.

(4) PROPRIETARY MAGAZINE. Another form of advertisement worth considering as an alternative to circulars on the part of a business house prepared to spend money somewhat freely, is to run its own paper or magazine. If a magazine can be so conducted as to pay its own expenses, the advertisements will then cost the firm nothing. Even if it is worked at a loss, the gain will be in the advertisements. Quite a fair number of magazines are now tied in this way to some particular concern, although great trouble is often taken to conceal the fact.

(5) POSTERS, ETC. Another form of advertisement is by way of posters or electric advertisements similar to posters. Here again the tendency seems to be for these to be the less effective as the quantity of them increases. The appeal here is a momentary one, for the majority of persons passing along a much frequented thoroughfare are unable to stop whilst they read the advertisement.

The advertising, not merely of hotels where one can get accommodation, but of towns or villages in which to spend one's holidays, has come more and more to the front of late years. Advertising of this kind, if carried out judiciously, will certainly pay so long as it remains an unusual thing to do. When it becomes general the return on the advertisement will be much less.

Some towns which are surrounded by plenty of land available for building purposes may find it a good proposition to spend a sum on advertisements. It may be the quickest way to get the surrounding land taken up and built on so as to increase the rateable value of the local authority itself, and in consequence its income.

In this country one way of arriving at the distinction between so-called professions on the one hand and trade and manufacture on the other is that members of professional bodies are not allowed to advertise.

In connection with what advertising is and what it does, it is interesting to ask why that should be the case. The explanation is probably to be found in the belief that the members of a profession would be worse off rather than better off, if they were allowed to advertise. It is a form of organisation designed to reduce the



working expenses of the members of a particular profession. If one member were to advertise all would have to advertise. Those in control of the largest amount of capital would spend most on advertisements, and if the advertising was really effective the greater part of the work would go to the longest purse rather than to those of the greatest abilities. On the other hand, if the advertisement was ineffective, it would be a waste of money.

**DRAFTING ADVERTISEMENTS.**—The chief points to be observed when drawing up an advertisement are—

(1) **SIMPLICITY.** An advertisement should express as much as possible in as few words as possible. For this reason a suitable catch title easily remembered is best ; e.g. “prevents that sinking feeling.”

(2) **ART.** An advertisement should attract and not repel, and consequently the artist is being increasingly sought after by advertisers.

(3) **APPEAL.** This depends a great deal on the section of the public appealed to ; for example, if it is the mothers of the land, as in the case of patent foods, the advertisement will have a strong human note, e.g. a healthy baby with a nurse ; while if the sporting section of the community is appealed to, say, an advertisement of cigars, a virile picture such as hunting incidents will be more successful.

(4) **EXPENSE.** This is a very serious consideration, and the article itself will often decide what proportion of the selling price can safely be expended on advertising. For example, the greatest part of the prime cost of a patent medicine is swallowed up in advertisements, whereas articles in which there is a great competition cannot stand much advertising expense.

(5) **MEDIUM.** This is also most important as the advertiser must consider through what medium he can reach the bulk of his prospective buyers, and an error of judgment will often entail a dead loss. The book-maker would not advertise in the *Church Times*, while a patent medicine manufacturer would be ill advised to advertise in the *Christian Science Monitor*. These are extremes, but the principle holds good throughout.

(6) **THE TIMELY REPETITION.** It is important that the right period be chosen for the advertisement ; it would be wrong to advertise furs in the summer, straw hats in the winter, etc. In many trades the best results are obtained at the Christmas season, Easter, or



Whitsuntide. The right time for advertising must naturally be chosen, but it must not be left until the last minute. Advertisements should be handed in several days before they are due to appear so that they can be carefully set up and placed in a good position—otherwise the advertiser must be content with any space which happens to be left over, and the compositor likewise cannot give the necessary care to the setting of the type. In holiday and health resorts the people have usually more time for reading than when at home or business—a fact which must be taken into consideration. The days of the week are also of importance. During the winter the Sunday papers are more carefully read than is the case in summer. Saturday is usually a favourable day for advertising, and so are Mondays and Wednesdays. The housewife is usually fond of reading the tales or serials which appear in the newspaper. If an advertisement appears immediately after such a serial, it has the best chance of attracting her attention. Advertisements of bankers and similar commercial concerns should appear in the commercial section of the paper.

### TEST PAPER XXI

1. What was the original meaning of the term "Advertising"?
2. Into what classes may advertisements be roughly divided?
3. Explain the real function of an advertisement.
4. What different forms may the advertising policy assume?
5. Name the various methods of appeal which are used in advertising.
6. Mention any peculiar forms of advertising which have come into prominence within recent years.
7. For what purpose does the advertiser use—
  - (a) Trade journals?
  - (b) The daily press?
  - (c) Monthly magazines?
  - (d) The hoardings?
8. Describe the various methods of propaganda which may be used by a retail firm. Which method is especially prominent at Christmas time?
9. What, in your opinion, would be the probable results of allowing the learned professions to advertise?
10. Mention any items of business expenditure which usually tend to increase the value of Goodwill.
11. "In normal times £100,000,000 a year is wasted in advertising in the United Kingdom." Give reasons for agreeing or disagreeing with the view that money spent in advertising is wasted.
12. Analyse the economic effects of advertising. Discuss the advantages to (a) the manufacturer, (b) the retailer, and (c) the customer of the advertisement of a given article.
13. You are about to open a retail establishment in your district. Describe the methods you would adopt to gain customers.
14. What are the chief points to be observed in drawing up an advertisement?

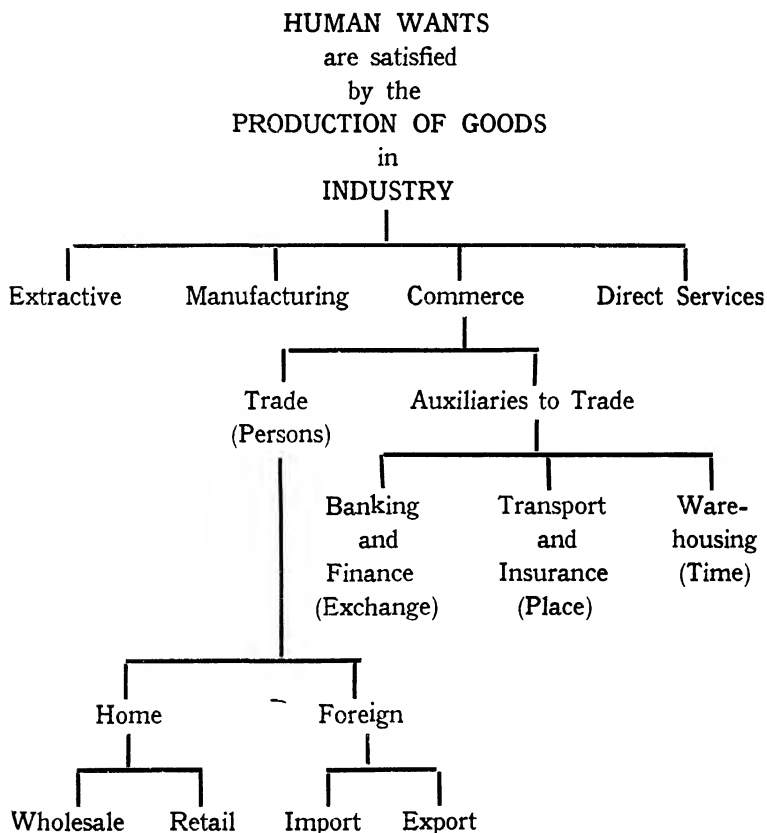


# SECTION IV—TRADE

## CHAPTER XXII

### THE CLASSIFICATION OF TRADE

THE various branches of commerce will be considered in the succeeding chapters, and the student is advised to keep before him the following diagram illustrating the various subdivisions of industry—



From the above it will be seen that "Commerce" forms a part



of "industry," and has already been defined as the sum total of those processes which are engaged in the removal of the hindrances of persons, place, and time in the exchange of commodities.

This definition will now be analysed under the following headings—

(1) **TRADE**—the means by which the *personal* hindrance is surmounted.

(2) **BANKING AND FINANCE**—the study of the mechanism by means of which exchanges are effected.

(3) **TRANSPORT AND INSURANCE**—the means by which the hindrance of place is removed.

(4) **WAREHOUSING**—the means by which the hindrance of time is overcome.

**TRADE.**—In the chapter on "Commerce as a branch of Production," it was pointed out that the object of trade is to surmount the *personal* barriers which would exist if the producers in a community were obliged to effect the exchange of their goods themselves. The Swiss watchmaker and the Australian farmer are both seen to enjoy each other's products, although the exchange is effected by the intervention of a *third* person, known as the trader. With the advent of the trader, each worker is enabled to concentrate his energies on his own particular branch of industry, so that the advantages of separation of employments is expressed in an increased output.

The function of the trader is the mediation of the exchange of goods between the producer and the consumer. An undertaking which is engaged in this form of mediation with the object of making a profit is described as a trader's business. The economic function of such an undertaking is to buy goods in the place where they are extracted or manufactured, and to direct them to places where they are required for consumption.

Trade, then, is the exchange of goods between different members of industry, and is usually effected by a specialised person. Trade may be divided into many different kinds, according to the point of view taken. The following are some of the most important bases on which the division may be made—

(1) THE NATURE OF THE COMMODITY TO BE EXCHANGED.

(2) THE SCOPE OR EXTENT OF THE BUSINESS UNDERTAKING.

(3) THE PERSON FOR WHOSE ACCOUNT THE BUSINESS IS UNDERTAKEN.



- (4) THE LOCAL AND GEOGRAPHICAL EXTENSION OF TRADE.
- (5) THE METHOD BY WHICH GOODS ARE BROUGHT INTO EXCHANGE.
- (6) THE DEGREE OF DEVELOPMENT OF THE TRADE FROM THAT OF A STATE OF BARTER.

**(1) THE NATURE OF THE COMMODITY TO BE EXCHANGED.—**

(a) *Trade in Raw Materials and Manufactured Goods.* This is a most important kind of trade, both historically and from the standpoint of the physical exertion involved. It is subdivided into a large number of smaller groups, embracing almost the whole of the extractive and constructive and manufacturing industries.

(b) *Trade in Published Works, Music, and Artistic Goods.* This is more concerned with the sale of products of the intellect, in the form of written and artistic works, magazines, newspapers, and inventions of all kinds.

(c) *Trade in Money, Bills, and Credit Instruments.* This is usually known as banking, and consists in the turnover of coins, paper money, uncoined gold and silver, the purchase and sale of bills, Consols and other Government securities, stocks and shares, and the loan of capital and of credit.

**(2) THE SCOPE OR EXTENT OF THE BUSINESS UNDERTAKING.—**

(a) *Wholesale Trade.* This is concerned solely with the distribution of large quantities of goods received directly from the manufacturers or dealers on the large produce exchanges, and sold in smaller quantities to others. The wholesale merchant buys from the manufacturer or producer in bulk and sells to the retailer in smaller quantities. He is the middleman between the manufacturer or producer and the retailer or shopkeeper. His buying is usually restricted to a group of articles more or less related to one another. For example, he may confine himself entirely to raw wool, cotton, tobacco, flour, cloth, tea, sugar, or any one of the numerous articles of commerce which are manufactured and sold on a large scale. The wholesale dealer is thus an expert in the class of goods in which he deals.

Two types of trader may be distinguished, namely—

(1) *The Wholesale Merchant*, who purchases his supplies from a number of markets, making his purchases outright and re-selling to the best advantage on his own account. He is concerned with the subdivision and dispersal among retailers of the produce



thus assembled, in the precise quantities and at the times desired by the retail trade.

(2) *The Wholesale Commission Salesman* who merely acts as a selling agent on behalf of distant producers, and whose primary function is to strike the best bargain possible on behalf of his clients. As a general rule, the activities of this type of dealer are restricted to the larger distributive centres. In some cases he advises the producer as to the state of the market, warning him when the forwarding of produce is inadvisable.

Frequently the line of demarcation between these two types is not clearly defined, and it is not unusual for the two operations of dealing on commission and on one's own account to be undertaken by one firm.

(b) *The Retail Trade*. This is concerned with the distribution of goods in *small* quantities to the consumers or users of the goods, and is thus in contradistinction to the wholesale trade. In practice, however, the border line between the two is not always clearly drawn. At times the wholesale merchant is also engaged in the retail trade. Moreover, the wholesale merchant is not always the more important or the more highly skilled as compared with the retailer, and the business of the latter is by no means always on a small scale.

The retail trade manifests itself in a variety of forms which may be divided into two main groups—

(1) *The Itinerant Trade*, which is a form of retail trade in which the seller has no fixed locality, but conveys his stock of goods from place to place. It is represented by hawking and peddling, street and market dealing.

(2) *Local or Fixed Trade*, which assumes the form of ordinary retail shops. Although the small undertaking is the predominant form, the large-scale concern has acquired increased importance in recent years in the large cities. Nevertheless, the small retailer still finds a large field for his activities in the sphere of distribution, since he serves a different section of the community.

**(3) THE PERSON FOR WHOSE ACCOUNT THE BUSINESS IS UNDERTAKEN.**—(a) *Trade on One's Own Account*, where the profit on the transactions is acquired by the person effecting the exchange.

(b) *Trade on Commission*, where the trader acts for the account and according to the instructions of another party, and is generally



remunerated by the payment of a fixed percentage on the amount of business done.

**(4) THE LOCAL AND GEOGRAPHICAL EXTENSION OF TRADE.—**

(a) *The Home Trade*. This refers to the buying and selling of goods for delivery within the boundaries of a particular country, and may be carried on by land or by sea, or along the coasts of the country from one port to another.

(b) *Foreign Trade*. This refers to the trade which traverses the boundaries of the home country and consists in a regular interchange of goods with the inhabitants of foreign countries, colonies, and dependencies. It is sometimes distinguished according to the part of the earth with which it is conducted, such as the East Indian, West Indian, Russian, Levant, or the American Trade.

(c) *The World Trade*. This has reference to the totality of the external trading relations of all the nations of the earth. Examples of commodities which give rise to a world trade are corn, sugar, coffee, tea, petroleum, wine, cotton, wool, wood, coal and iron.

FOREIGN TRADE may be divided further into—(a) *The Import Trade*, which consists in the procuring of foreign goods for home use.

(b) *The Export Trade*, which consists in the supply of home goods for foreign use.

(c) *The Entrepôt Trade*, which effects the exchange of goods between foreign producers and foreign consumers. Under this heading would come the transshipment trade.

**(5) THE METHOD BY WHICH THE GOODS ARE BROUGHT INTO EXCHANGE.—**(a) *Land Trade*. Under this heading belongs especially Caravan Trade, which takes place when merchants combine in caravans, with armed attendants for protection against highway attacks on their journey through deserts and other insecure areas. For the same reason, there existed at an early period fleets of merchant vessels escorted by a ship or ships of war, and trade carried on under such circumstances was known as Convoy Trade. Under the heading of Land Trade must also be included that of railways, rivers, canals, and inland seas.

(b) *Sea Trade*. This includes the trade with oversea countries and, therefore, embraces that done with our colonies and dependencies.

(c) *Coastal Trade*. This signifies all the trade by sea from any one port of the home country to any other port thereof.



**(6) THE DEGREE OF DEVELOPMENT OF THE TRADE FROM THAT OF A STATE OF BARTER.**—Barter is the exchange of commodities directly for other commodities, without the use of any intermediate substance such as money. An interesting case of barter is to be seen at the British Museum in the counterpart of a deed of conveyance of land at Port Philip, now the site of Melbourne, dated 6th June, 1835, from the native chiefs to John Batman, founder of Victoria Colony. The land was given in exchange for 20 pairs of blankets, 30 tomahawks, 100 knives, 50 pairs of scissors, 30 looking-glasses, 200 handkerchiefs, 100 lb. of flour ; with a yearly rent of 100 pairs of blankets, 100 knives, 100 tomahawks, 50 suits of clothing, 50 looking-glasses, 50 pairs of scissors.

Barter is still exercised in the trade with the West African natives. It can exist, however, only in a very simple state of society. As stages removed from barter may be distinguished—

(a) *Domestic Trade*, in which goods are made in the homes of the workers, mainly by hand, as in the case of the tinker, carpenter, shoemaker, and then held by them until the time of sale.

(b) *Manufacturing Trade*, in which goods are made and then kept for sale by the manufacturer, as in the case of machines, cigarettes, etc.

(c) *Mercantile Trade*, in which the goods offered for sale have been derived either directly or indirectly from another party, who acted as the producer.

### TEST PAPER XXII

1. Copy the diagram on page 237 and explain its meaning.
2. Define "Commerce" so as to bring out its main functions.
3. Name the four main branches of Commerce and state the object of each.
4. Describe briefly the services performed by the trader on behalf of the community.
5. Upon what bases may "trade" be classified?
6. How may "trade" be divided according to the nature of the commodity exchanged?
7. Which, in your opinion, is the most useful and convenient method for the classification of trade?
8. Distinguish between "local" and "distant" trade.
9. Trade is usually divided into "Wholesale and Retail"; "Import and Export." Point out briefly the principal defects of this division.
10. Explain how trade may be divided according to its degree of development.
11. Distinguish the function of the wholesaler from that of the retail trader, and state the services rendered by the former to the latter.



## CHAPTER XXIII

### CHANNELS OF DISTRIBUTION

**CHANNELS OF DISTRIBUTION IN THE HOME TRADE.**—Under the present system of market distribution, merchandise ordinarily passes through the hands of one or more middlemen between the producer and the consumer. Prior to the Industrial Revolution, direct sale to the consumer was the normal method of disposing of the majority of commodities. As the scale of industry increased and it became more specialised, more highly localised and more complex, the need for one, and often for several, middlemen made itself felt, and the marketing system grew in complexity. The seller must devote considerable care to the selection of the proper method of distributing his product. Conditions change, and new types of middlemen come into existence or increase in importance, while old types lose ground in the competitive struggle. Again, the demand for a product changes. Thus, a new product may be marketed by the direct mail method, but when it becomes known the retail stores may offer a larger outlet. A wide variety of methods are in use, not all of which are open to every seller, but the following are amongst the most important—

(1) **Direct Sale to the Consumer.** Although the growth of specialisation has created numerous trading intermediaries, the stress of competition has in certain cases caused producers to undertake all the services which it was once the merchant's special task to perform. Direct selling has been approached along two very different lines. On the one hand, manufacturers have devised entirely new methods of distribution, by house-to-house canvassing or by mail order; on the other they have themselves established special departments to carry on the ordinary business of retailing through their own chains of shops. In certain cases direct sale is a comparatively simple matter as, for instance, in the industries producing capital goods. Manufacturers of locomotives or electrical generating plant can sell direct to the consumer, since demand is not dispersed among the general population, but is concentrated at comparatively few points. Direct sale may also occur between grower and consumer in the marketing of agricultural produce. This method appears



to be generally successful where the small producer hawks his produce in the nearest town, or, to a less extent, through the medium of a retail shop or a stall in the local market. Direct sale is mostly undertaken by growers situated within driving distance of a town of sufficient size to provide an adequate and regular outlet for the whole of the produce. The varieties raised must be sufficiently diverse to enable the grower to supply the greater part of the needs of his customers, but difficulties inevitably arise, such as non-continuity of supply and the unforeseen requirements of customers, which compel the grower at times to purchase produce for resale in order to maintain his connection.

(2) **Direct Sale to Retailer.** The next shortest trade channel is followed when the goods pass through the hands of one middleman, i.e. the retailer, between the producer and consumer. The sale of farm produce for local consumption provides the most familiar and the longest established example of direct sale by the producer to the retailer. It is a well-established custom for the larger growers of mixed crops within easy driving distance of large towns to organise the sale of their own produce and dispose of it to retailers at the wholesale markets. A much more recent development, however, is the growth of direct sale to the retailer by manufacturers who are producing for the general market. This tendency to eliminate the wholesaler manifests itself in a variety of forms. It may be due to the initiative of the manufacturer who sends his own travellers to the retail shops. On the other hand, it may be due to the large retailer who sends his buyers to the manufacturer, or who, by establishing a chain of stores managed from a central office and served by a central buying department and warehouse, virtually sets up his own wholesaling organisation. When the initiative comes from the side of the manufacturer, certain conditions must be fulfilled before a policy of direct sales to retailers can succeed—

(a) The manufacturer must produce on a large scale in order to make it worth his while to organise such a method of distribution. He must also possess the necessary capital to finance the marketing operations.

(b) The demand for the article must be constant throughout the year. It is not worth maintaining one's own sales force if it cannot be employed the whole year round because of sharp seasonal fluctuations of demand.



(c) Direct sale will be impossible if the manufacturer is a specialist whose products are only bought in limited quantities by each individual retailer. This does not apply to expensive specialities which are only stocked by a limited number of high-class dealers.

(d) The manufacturer with a "full" line of goods is most likely to be successful with such a policy. The expense of a salesman handling many articles can be spread amongst them, thereby reducing the burden on each.

**(3) Sale to Wholesalers.** Wholesalers have for many years been established as middlemen through which many goods pass between the manufacturers and the retailers. The wholesaler most commonly retains his position of importance in the sale of bulk goods which are manufactured on a small or moderate scale and which are neither proprietary nor branded articles, and in whose disposal advertising to the consumer consequently plays little or no part. Among the more obvious examples of such goods are the commoner kinds of glass and china, hardware, and textile fabrics. The wholesaler has a sales force calling upon retailers regularly, and usually has lower selling expenses than the manufacturer who sells direct to retailers, since his sales force represents many manufacturers. He also performs many of the other marketing functions, such as assembling, storage, and finance. From the point of view of the manufacturer, however, an over-dependence upon the wholesaler causes him to lose contact with retail dealers. Again, many wholesalers have so many products to sell that they are unable to push the sales of all goods carried in stock. The wholesaler, too, may at any time discontinue one manufacturer's line to take over a competitive line, or to put out his own branded goods. In using this channel, therefore, the manufacturer must consider whether he can perform the wholesale functions or services, and whether he can perform them better or cheaper than the wholesaler. If his product requires aggressive salesmanship, he may find it desirable to go direct or to make arrangements with selected wholesalers under which they will put real sales effort behind his product.

**(4) Exclusive Agencies.** Manufacturers often sell through a limited number of dealers who are granted exclusive agencies in their respective territories. The agency contract may require the dealer to buy certain minimum quantities of merchandise, whilst the contract may be made to cover a definite period, or it may be for



an indefinite period, either party having the right to cancel it at any time upon due notice. The main argument in favour of exclusive agencies is that they get more interest and more sales effort from the dealers, so that the volume of sales is increased. The dealer with an exclusive territory has more interest in the product; he advertises it more, as he feels that no other dealer will profit at his expense. Exclusive agencies are more likely to be used with "shopping" products than with convenience goods. They are desirable when service is important, or when the manufacturer wishes to control the merchandising policy of the dealers.

(5) **Sales Through a Manufacturers' Agent.** The producer who does not wish to give up direct contact with his customers, and who wants to be represented permanently in a certain area, but who wishes to avoid the expense of a branch, will engage a suitable agent. Such an agent has the advantage that he is familiar with the business conditions of his district, and that he knows a number of prospective customers. Especially in large cities, where demand is great and the occasional visitation of customers by travellers is not sufficient, permanent representation by an agent is to be preferred. The manufacturers' agent does not act in his own name, but in the name of his principal, on whose behalf he enters into dealings with customers. He has a contractual relationship only with his principal. This relationship is generally entered into for an indefinite period, so that during its existence the agent is permanently engaged in safeguarding the interests of his principal.

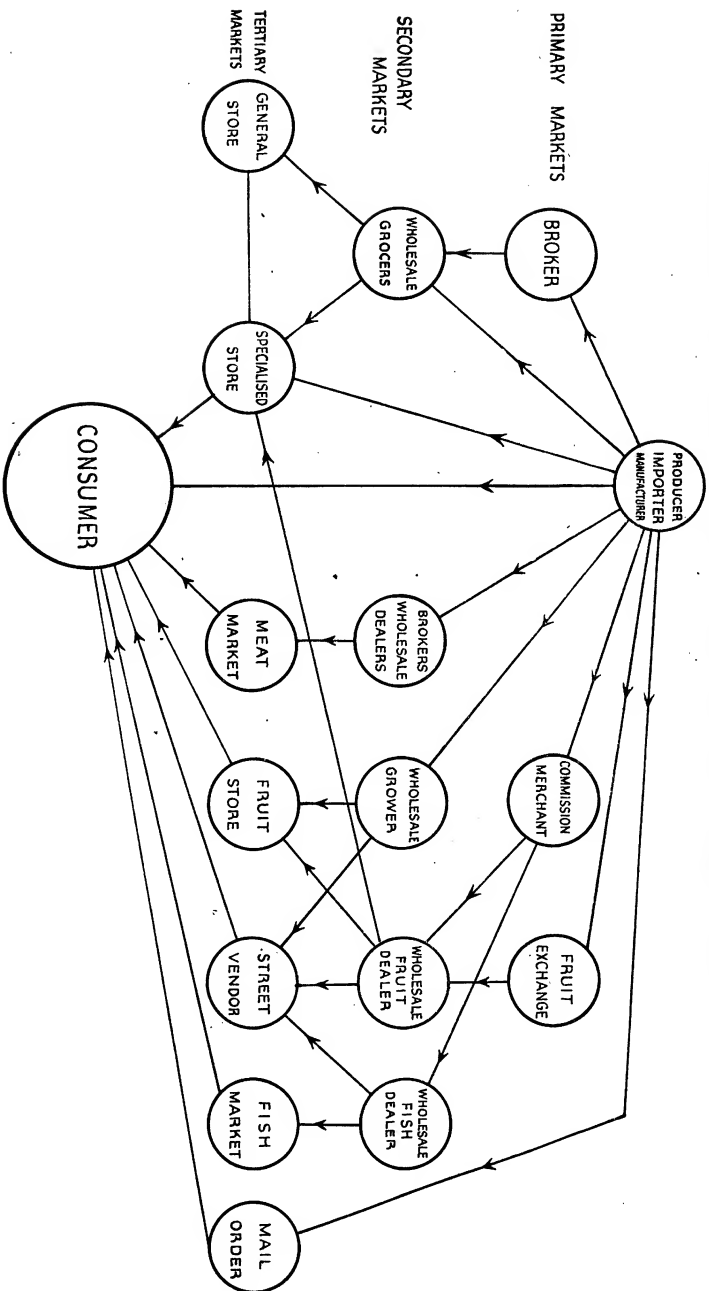
(6) **Sales Through Commission Agents.** The existence of these agencies is frequently due to a specialisation of function in the wholesale trade. Such agents are frequently employed in the marketing of agricultural produce. This agent concludes all business in his own name, so that the relation between the principal and the commission agent does not concern the third party at all. This mode of trading is illustrated by the work of the commission salesman in the fruit and vegetable trade. This salesman, who frequently sells to a wholesaler, endeavours to strike the best possible bargain on behalf of his clients. In addition to the actual service of finding customers, the salesman usually supplies the grower with the bags, baskets, or other containers in which the produce is packed and pays on the grower's behalf any freight or other charges which may be due.







# CHANNELS OF FOOD DISTRIBUTION IN THE HOME TRADE









In some cases he advises the grower as to the state of the market, warning him when the forwarding of produce is inadvisable; he also accepts responsibility for any bad debts which he may incur in the process of sale. For his services he charges a commission on the selling price, or occasionally a flat rate on a quantitative basis, this remuneration being deducted from the price realised, together with other incidental charges such as rail transport, cartage, portage, market dues, and a charge for the use of empties.

The various channels through which supplies of foodstuffs reach the ultimate consumer in the home trade are shown in the inset between pages 246 and 247. It will be seen that the primary markets consist of intermediaries proper whose function is to direct the foodstuffs from the home grower or importer into wholesale channels. These are indicated on the diagram as Secondary Markets, since they receive their supplies at second hand and for the most part are not in direct contact with the producer or importer. They are, however, conveniently situated to serve the needs of the various types of retail trade which are described collectively as Tertiary Markets. Elimination is possible at every stage, the most direct route being that between producer and consumer, in which case there are no intervening links.

**CHANNELS OF DISTRIBUTION IN THE EXPORT TRADE.**—There are many complications in the export trade which do not occur in the case of trade in the home market. Supplies must be adapted to the special needs of peoples with whom the exporter is not in touch; there are customs, traditions and prejudices peculiar to every race, which in many cases affect the sale of goods. Questions of freight and packing have outstanding importance; customs charges vary considerably in the different countries; and finally, the modes of payment, which again are subject to many variations, must be carefully ascertained. All these things have no parallel in the home market and demand careful consideration. The export trade, as a branch of intermediary trade, may be conducted either on one's own account or on a commission basis. From the point of view of the manufacturer, the export trade may be undertaken by the direct or the indirect method. Where direct exporting is decided upon, the manufacturer exploits his own markets, chooses his own methods of developing business and shoulders the entire responsibility for all operations. Under the indirect method, the



work is handed over to some specialised intermediary. The following are the principal channels of export—

(1) **Manufacturer's Export Department.** Direct exporting, that is to say, the exportation of goods by the manufacturer to the importer on the one side, is as a rule only economical when the manufacturer is in a sufficiently large way of business to enable him to establish an export branch in connection with his own sales department. The export business presents so many peculiar problems that it is best for a manufacturer to handle the whole of his export business through a separate department. He may then proceed to open up relations with his market through the medium of travelling salesmen. The success or failure of the manufacturer working on these lines will depend just as much upon the qualifications of the persons he sends overseas, as the quality, utility, or price of his wares. The personal element is just as important a factor in the foreign as in the home trade. A second means of opening up foreign markets is through the medium of correspondence. This is an economical way of commencing business, but it demands the highest qualifications of the man who is conducting the campaign.

(2) **Foreign Branches.** In the case of large businesses, manufacturers have established foreign branches as a means of opening up a direct connection with an overseas market. This method has the supreme advantage of enabling the concern to maintain a close contact with conditions in the market. Credit problems are reduced to a minimum, since the man in charge can investigate, on the spot, the customer's capabilities for meeting his obligations. In Canada, for example, some firms have established branches in charge of a manager, with control of salesmen and stocks at one or more points. This policy has been adopted in trades such as tool steel, food products, and chemicals. In other cases the Canadian branch has had the benefit of repair shops, as in the case of the trade in machine tools and electric motors. Under such a policy it is necessary to have an adequate selling organisation, stocks at important points, and total overhead expenses in a proper relation to the business available. Several firms have allowed their rentals, salaries, and general expenses to overshadow the volume of business transactions.

(3) **Joint Selling Associations.** The formation and maintenance of an export department, or the operation of foreign branches, requires a considerable expenditure of capital, which is justified only when



the amount of business done with overseas customers is exceptionally large. If, however, the cost of maintaining a branch and of carrying stocks is more than a given article will bear by itself, the obvious solution is for a number of firms manufacturing allied articles to share such overhead expenses in their common interest—in other words, to form a joint sales organisation. Thus, in the Brazilian trade, Continental and United States manufacturers have opened showrooms for their agents and have deposited goods on consignment in charge of capable men sent out to demonstrate them. This has been made possible by the combination of manufacturers whose products, not competing with each other but related in character, are capable of demonstration together in the same showroom. Each firm contributes to the upkeep of the showroom and the orders which are taken are handed to the respective manufacturers of the goods. Experts attached to these depots, which are especially suitable for machinery or engineering products, are prepared to furnish plans and information as to the working of new machinery. British firms have shown themselves slow to adopt this form of organisation, though such an association exists in the machine tool trade.

(4) **The Merchant Shipper.** This type of export organisation has a longer tradition than any other, for it is the pioneering form which Great Britain adopted to lay the foundations of her overseas trade. Export merchants of this class, trading on their own account still play an important role in international trade. It is especially when dealing with backward countries, in which commercial and banking facilities are not well developed, and where the financing of business presents many difficulties, that the export merchant is a most useful intermediary. His position has been materially weakened in those places where there are large importing firms possessing sufficient capital and credit to enable them to deal directly with foreign manufacturers. The merchant system has the danger to the manufacturer that it prevents him from becoming fully acquainted with the requirements of his market. Yet, in spite of this, the merchant shipper performs valuable functions, as in the case of the cotton trade, where—

(a) He finances the goods from the time they leave the manufacturer, through the finishing processes, until after they have been sold in the country to which they have been exported.



(b) He has to know from what manufacturer he can obtain particular kinds or qualities of goods and where to secure the particular finish that is required.

(c) He must have intimate knowledge of the requirements of the markets in which he trades, and of all the conditions. He must also pay careful attention to packing and shipping arrangements.

(5) **Export Commission Houses.** These are primarily representatives of foreign importers on whose behalf they act in the exporting country. Their main function is the purchase of goods in accordance with instructions received from foreign concerns, the latter paying them a commission for their services. These firms are familiar with the best sources of supply from which they may obtain the goods needed by their clients abroad, their information being kept up to date by special investigations as well as from trade periodicals, etc. Buying instructions which they receive from abroad may be either to purchase from a named concern, or to place the order wherever they may obtain the most advantageous terms. Owing to the increase in the number of widely advertised trade-marked and branded goods, the trend is towards making instructions from abroad specific, thus leaving little room for the exercise of discretion on the part of commission houses.

(6) **Manufacturers' Export Agents.** There are various types of manufacturer's export agencies. Some agents have no extensive organisations; they are individuals residing in a seaport and having for their function the distribution of catalogues, circulars and price lists among firms engaged in exporting; other agents are established in foreign countries where they act as resident salesmen for a group of manufacturers; still others are large concerns having extensive selling, shipping, and financing departments, and maintaining an office at one or more of the large ports. A great deal of the British export trade is done through agents in overseas markets. It is stated, however, that a certain amount of trade is lost to this country each year through insufficient care on the part of British manufacturers in the selection of their agents abroad, and through defective supervision of the agents when appointed. The disadvantage of placing one's export sales in the hands of an export selling agent is due mainly to the fact that he represents an independent organisation; he is not an employee of the manufacturer whose sole interest is the development of the latter's business. An agent



often works on a time contract, and seeks immediate results irrespective of whether the sales make or do not make a solid foundation for the growth of the manufacturer's export trade. Such an attitude of exporter's agents is to some degree justified by the loss of accounts which many of them sustain after they have done some valuable initiatory work, the manufacturer then deciding that he wants to assume direct control of his foreign trade.

### TEST PAPER XXIII

1. Enumerate briefly four different channels of distribution which may be adopted by the producer in the disposal of his goods to the home consumer.

2. State concisely the conditions under which it is advantageous for the producer to sell directly to the consumer.

3. What are the conditions which must be fulfilled before a policy of direct sales by the manufacturer to the retailer can succeed?

4. If all wholesale business were abolished and goods were sent directly to the retailer from the producer, in what ways would the shopping public probably be affected?

5. What is the advantage to a manufacturer of granting exclusive agencies to a limited number of dealers?

6. What functions are performed by (a) manufacturers' agents and (b) commission agents, in the distribution of goods between the producer and the consumer?

7. "A business man, in these days, is a specialist, whose services in the placing of goods are as important as those of the technical expert in their production." Comment upon this statement.

8. Classify the types of middlemen who may intervene in the passage of goods from home producer to home consumer, and point out the reasons for the existence of each of the types you mention.

9. Enumerate three important channels of distribution employed by the home manufacturer in the export of his goods abroad.

10. Under what circumstances is it advisable for a manufacturer to establish an export branch in connection with his own sales department?

11. What justification is there for the establishment by a manufacturer of a branch in a foreign country?

12. Show the necessity for the following in the export of merchandise, and put a reasonable limit to their operations—

(a) The merchant shipper.

(b) The export commission house.

(c) The manufacturers' export agent.

13. Discuss the extent to which association of producers are in a position to eliminate the independent middleman.

14. "One of the root causes of the world situation at the present time is the fact that we have solved during the last hundred years the problem of production, but we have not solved the problem of distribution." Comment on, and consider the adequacy of, this diagnosis.



## CHAPTER XXIV

### THE PURCHASE AND SALE OF GOODS

THE success of a trader's business depends to a large extent upon the manner in which the purchase of the stock is effected: the more favourable the buying, the easier and more beneficial will prove the sale. The old adage is "Goods well bought are already half sold." Mistakes in buying find their own redress. Where the tastes and requirements of the customers are wrongly anticipated, the goods may prove altogether unsaleable. Sudden changes in fashion, new inventions, and unemployment may also prevent the sale of goods.

Since all buying is effected with a view to subsequent sale, it follows that both buying and selling are activities which should be carried on in the closest co-operation. In some undertakings the person in charge of the buying is also responsible for the selling, but whether this is the case or not, the buyer should possess an intimate knowledge of the merchandise in which he deals, as well as of the legal principles involved in buying and selling.

**GENERAL CONDITIONS OF PURCHASE.**—The main factors which the trader has to consider when making his purchases are the quantity, quality, price, payment, packing, and the time of delivery of the goods.

**Quantity.** The quantity of goods purchased by the retailer will naturally vary with the conditions of the market. It is the duty of the seller to deliver the exact amount which has been ordered. In the event of the delivery of a wrong quantity, the rules, subject to any usage of trade or special arrangement of dealing between the parties, are—

(1) Where the seller delivers to the buyer a quantity of goods less than he contracted to sell, the buyer may reject them. But if the buyer accepts the goods so delivered he must pay for them at the contract rate.

(2) Where the seller delivers to the buyer a quantity of goods larger than he contracted to sell, the buyer may either—

- (a) Accept the goods ordered and reject the rest, or
- (b) He may reject the whole.



If he accepts the whole of the goods so delivered he must pay for them at the contract price.

(3) Where the seller delivers to the buyer the goods he contracted to sell mixed with goods of a different description not included in the order, the buyer may—

(a) Accept the goods which are in accordance with the contract and reject the rest ; or

(b) He may reject the whole of the goods.

**Quality.** There is an infinite variety of materials all differing in quality. After they have been collected from the extractive and manufacturing industries, they are next assorted and classified into different qualities, and may then be regarded as merchandise in the truest sense of the word. The goods are mixed, cut, refined, etc., and then grouped into recognised types each having its different characteristics. One of the most important points in a contract of sale is the determination of the exact quality which the buyer has in mind.

With regard to the quality of the goods, including their state or condition or their fitness for any particular purpose, there is no implied warranty or condition except as follows—

(a) An implied warranty or condition may be annexed by the usage of trade or by the provisions of a particular statute, e.g. The Merchandise Acts, 1887.

(b) Where the buyer makes known to the seller the particular purpose for which the goods are required so as to show that the buyer relies on the seller's skill or judgment and the goods are of the description which it is in the course of business to supply, there is an implied condition that the goods shall be reasonably fit for such purpose.

The *quality* is usually indicated by the buyer in one of the following ways—

- (1) General description of the goods.
- (2) Sample or pattern.
- (3) Analysis.
- (4) Type.
- (5) Trade Mark.

**DESCRIPTION.** In the case of a contract for the sale of goods by description there is an implied understanding that the goods shall correspond to the description. Particular qualities of goods have



particular descriptions, such as Yorkshire Hams, Paisley Flour, English Cheddar, Japanese Silk ; and when such goods are ordered the contract is fulfilled only when the commodities answer to their description. Sometimes goods are sold by sample or pattern as well as description, e.g. 200 yd. Japanese Silk No. 879, where the number indicates the particular pattern of the silk. In this case it is not sufficient if the bulk of the goods correspond with the sample if they do not also correspond with the description.

**SAMPLE OR PATTERN.** A sample is a small quantity of an article produced by the buyer as a specimen of the goods desired. A great variety of merchandise such as sugar, spirits, wine, coffee, etc., is sold by sample. A pattern is a specimen of a manufactured article such as cloth, paper, silk, leather, etc. When goods are sold by pattern or sample, the seller guarantees that the goods shall at least equal, on an average, such sample or pattern. In the case of a contract for sale by sample or pattern three conditions are implied—

(a) That the bulk shall correspond with the sample or pattern in quality ;

(b) That the buyer shall have a reasonable opportunity of comparing the bulk with the sample or pattern ; and

(c) That the goods shall be free from any defect rendering them unmerchantable which would not be apparent on a reasonable examination of the sample.

**ANALYSIS.** Many products are sold upon analysis, that is to say, on the basis of a determined quality, so that the exact composition of the goods supplied is arrived at by the analyst. In this case a provisional invoice is first prepared, until the results of the analysis are known, when a definite invoice is made out. If the quality of the goods delivered is inferior to that stipulated in the contract, a proportional allowance is made ; if it is superior, then there is a proportional increase in the price. As a rule, the contract gives the name of a chemist who is to be entrusted with the analysis, whilst in the case of many products there are special laboratories whose certificates of analysis are accepted without question. The copy of such a certificate is shown on the next page.

**TYPE.** When goods are sold “to arrive”—as in the case of corn, coffee, rice, etc.—their quality is determined according to



## CERTIFICATE OF ANALYSIS

We hereby certify that we have examined the undermentioned sample of

220 CASKS TALLOW

Sampled by us and averaged in proportion of the weight of each cask.

Marked-----*See back hereof for marks*

From---*Messrs. Shimmin & Sons*-----

and find it to contain—

0·68% water

0·12% dirt, mineral and other matter

0·80

(Signed) per pro.

JOHN KEENE & SON,

J. S.

type. This is a standard sample taken from the crop in the early part of the season, and the year's growth is guaranteed to be equal to the type. Should the produce prove to be inferior, an allowance is usually made, the amount being settled by arrangement or by arbitration.

**TRADE MARK.** Goods, and especially manufactured goods of small value, tend more and more to be sold according to *trade mark*. The mark signifies the quality of the articles and facilitates the task of the purchaser; he knows that on demanding an article of a certain mark, he will receive a definite quality which will meet his needs. Hence, there is no need to spend time in selecting the goods.

**Price.** In a contract of sale, the price may be fixed by the terms of the contract, or may be determined by the course of dealing between the parties; and in other cases a reasonable price must be paid. The price is based upon two factors, viz. a variable quantity of money, and a fixed and constant unit of weight or of measure. The unit of sale varies with different commodities, and usually decreases according as the value of the goods



becomes greater. In consequence of increased competition, other factors enter more and more into price, and the successful seller gives as little trouble as possible to the buyer in the quotation of his prices. Hence, the custom has developed of quoting prices inclusive of carriage, Customs duties, packing, etc., which are incidental to the purchase.

**Payment.** The payment of the price of the goods might be made immediately or after the expiration of a fixed period of time. C.O.D. (i.e. Cash on Delivery) terms are such as compel the buyer to pay for goods immediately before they are handed over to him. "Prompt Cash" means payment practically as soon as the goods are delivered. In actual practice, it allows time to examine the goods; and whilst in no case should it exceed seven days, the average time is three days. "Net" or "Ready Cash," sometimes termed "Cash," means settlement within a period of ten days. In case there is a discount, this is deducted from the invoice or statement before the account is paid. In many trades the cash discount is  $2\frac{1}{2}$  per cent and it is usually allowed if payment is made within one month.

**Cash Discount** is a deduction from the invoice price, which is granted to the buyer when payment is made in cash or before the expiration of a customary period of time. This form of discount is to be distinguished from *Trade Discount*, which is given either as a custom of the trade or on some special consideration, such as the taking of large quantities. In many wholesale trades, it is usual for the catalogue price of the goods to remain stationary; but when the market rises or falls, the trade discount is reduced or increased. In reality, trade discount represents the retailer's profit, and is deducted from the invoice prior to entry into his books of account.

**Packing.** In the case of many manufactured articles of general consumption, packing plays a most important part. Its object is not only to protect the goods from damage, but also to induce their sale. When goods are sold in packages or cases, there are three distinct weights to be taken into consideration—

(1) The actual weight of the goods, which is known as the *Net Weight*.

(2) The combined weight of both goods and package—known as the *Gross Weight*.



(3) The weight of the package in which the goods are enclosed—known as the *Tare*.

In most trades there is a recognised allowance made for the tare of the case, cask, chest, or other package in which the goods are secured.

*Actual Tare* means that the package has been weighed separately from the goods before they were packed; *Average Tare* is taken where the packages are numerous, and of a similar size or shape, and only a few have been weighed to form an average for the whole; while *Customary Tare* is an established allowance made in some trades for the weight of packages which are so invariably alike, and of such uniform weight, as to warrant a fixed percentage allowance being made for them.

**Time of Delivery.** Delivery may be made at once or within a certain period of time. Wholesale and retail traders engaged in the home trade endeavour to stock goods in order to meet the demands of their customers as they arise. This is not usually the case, however, with regard to the manufacturing trade nor with the import and export trade. The manufacturer usually keeps a reserve of raw materials and arranges for further quantities to be delivered at regular intervals. In the export trade, the time of delivery is based on the date of the ship's departure. In the import trade, *spot transactions* are those in which the goods can be delivered immediately. When the goods are sold *To Arrive*, it means that they are in course of transit from abroad, and will be delivered on the arrival of the vessel by which they are being conveyed.

**LEGAL MEANING OF "GOODS."**—For the purposes of the Sale of Goods Act, 1893, the term "goods" means all chattels personal other than money and things or choses in action, such as shares, debentures, bills of exchange, and promissory notes. The term also includes—

(a) Emblements, i.e. those vegetable products of the soil which are produced annually, not spontaneously, but by the labour and industry of the cultivator; such as corn and grain of all kinds, hemp, flax, hops, and potatoes.

(b) Things attached to land or forming part of the land, which are agreed to be severed either before sale or under a contract of sale, e.g. the timber in trees which are still standing at the time



of the transaction, whether it is sold at so much per foot, or at a fixed price, and whether it is to be cut by the seller or the buyer.

It will be seen that the legal meaning is much narrower than that of "economic goods," which is given on page 25.

**KINDS OF GOODS.**—The goods which form the subject of a contract of sale may be either—

(1) Existing goods, i.e. goods which are owned or possessed at the time of the contract of sale, or

(2) Future goods, i.e. to be manufactured or acquired by the seller at some future time after the making of the contract.

The goods, again, may be either—

(a) Specific or ascertained goods, i.e. goods identified and agreed upon at the time when the contract of sale is made, or

(b) General or unascertained goods, i.e. goods not so identified but described or referred to by the parties in general terms.

Where there is a contract for the sale of specific goods and the goods without the knowledge of the seller have perished at the time when the contract is made, the contract is void, e.g. if A contracts to sell to X a cargo of corn on board a ship which is supposed to be then on its voyage but which is in fact lost, the contract is void.

Where there is an agreement to sell specific goods and subsequently the goods without any fault on the part of either the seller or the buyer perish before the risk passes to the buyer, the agreement is thereby avoided; e.g. if A agrees to sell X 10 tons of potatoes to be grown on a particular farm and the crop fails, the agreement is avoided.

**FORM OF CONTRACT OF SALE.**—A contract of sale may be—

(1) In writing; or

(2) By word of mouth; or

(3) Partly in writing and partly by word of mouth; or

(4) Implied from the conduct of the parties.

But in accordance with the provisions of Section IV of the Sale of Goods Act, 1893, a contract for the sale of any goods of the value of £10 or upwards will not be enforceable by action unless—

(1) The buyer accepts part of the goods so sold and actually receives the same. There is an acceptance of goods within the meaning of this section whenever the buyer does any act in relation to the goods, which recognises a pre-existing contract of sale, whether there be an acceptance in performance of the contract or not; e.g. if goods sold are delivered



to the buyer, who takes a sample from them and, after examining it, says that the goods are not equal to his sample and that he will not have them, there is an acceptance for the purposes of this section of the Act, even though the buyer may still have the right to reject the goods as not being equal to sample.

(2) The buyer gives something in earnest to bind the contract or in part payment. Earnest consists of any coin or thing of value which is given in token of the bargain, but which is not, as a rule, part of the price; and part payment means an actual payment of part of the price in acknowledgment of the contract set up.

(3) Some note or memorandum in writing of the contract is made and signed by the party to be charged or his agent.

The Sale of Goods Act does not require the contract itself to be in writing, but there must be a memorandum of the contract. The memorandum must designate—

- (1) The parties, either by name or description;
- (2) The goods sold;
- (3) The price if agreed upon; and
- (4) The nature of the promise of the party to be charged.

The following will serve as an example as to what the memorandum must contain—

LONDON, 7th April, 19...
Dear Sir,
I beg to offer you £950 for your leasehold house at 23 The Lodge Drive, Palmer's Green.
Yours faithfully, GEO. HOLDEN.
J. SELLERS, Esq.

In 1893 Parliament passed an Act, known as the Sale of Goods Act, which collected into one code all the rules relating to the purchase and sale of goods in this country. All the general rules of the law of contract apply to it, so that there must be competent parties, good consideration, mutual consent, and all the other elements necessary for the validity of any other kind of contract.

**NATURE OF A CONTRACT OF SALE.**—A contract of sale of goods is a contract whereby the seller either—

- (a) transfers, or
- (b) agrees to transfer



the property in goods for a money consideration called the price. Hence the term "Contract of Sale" includes—

(1) Cases where the property in the goods is at once transferred from the seller to the buyer under and by virtue of the contract of sale, in which case the transaction is called an "executed" contract of sale, or a "sale" simply.

(2) Cases where the transfer of the property in the goods is to take place at a future time only, or subject to some condition afterwards to be fulfilled, in which case the transaction is called an "executory" contract of sale or an "agreement to sell."

But an agreement to sell becomes a sale when the time elapses or the conditions are fulfilled subject to which the property in the goods is to be transferred. Similarly a seller means a person who : (a) sells, or (b) agrees to sell ; and a buyer means a person who : (a) buys, or (b) agrees to buy goods. The distinction between a sale and an agreement to sell is important in at least three respects—

(1) Where goods have been sold and the buyer makes default, the seller may sue him for the contract price. But where an agreement to buy is broken, the seller's remedy is an action for damages. He cannot sue for the contract price because the property in the goods has not passed.

(2) If an agreement to sell is broken by the seller, the buyer has only a personal remedy against the seller because the goods are still the property of the seller, so that he can dispose of them as he likes ; and if he becomes bankrupt, they pass to his trustee in bankruptcy, who may, if he so choose, disclaim the contract. But if there has been a sale, the buyer has the usual proprietary remedies in respect of the goods themselves, and in many cases can follow them into the hands of third parties.

(3) If there is an agreement for sale and the goods are destroyed, the loss falls on the seller ; but if there has been a sale, the loss usually falls on the buyer, even though the goods may never have come into his possession.

In order that a transaction may amount to a contract of sale, the consideration for the contract must be money, either paid or promised, which is called the *price*.

Where the consideration for the transfer of the property in goods from one person to another consists of other goods, the contract is not a contract of sale but a contract of *exchange* or *barter*. Where goods are transferred from one person to another without any price or other consideration being given in return, the transaction is called a *gift*.

In the above example all the conditions required by the Act are satisfied—the parties, the description of the goods, and the price.



But the memorandum may consist in various letters, papers, or documents provided they are connected, consistent, and complete on the face of them. That is to say, the terms of a contract of sale need not be expressed in the same document, and it is permissible to prove a memorandum of the contract sufficient to satisfy the requirements of the statute from several documents or from a correspondence between the parties, but the connection of the various terms must be made out from the documents or letters themselves and may not be shown by oral evidence.

The requirements of Section IV of the Sale of Goods Act apply equally to executory as to executed contracts of sale. That is to say, every contract of sale of the value of £10 or upwards must comply with the provisions of Section IV notwithstanding—

(1) The goods may be intended to be delivered at some future time.

(2) The goods may not at the time of the contract be actually made, procured, or provided, or fit or ready for delivery, or

(3) Some act may be requisite for the making or completing of the goods or rendering them fit for delivery.

**RIGHTS OF THE BUYER.**—The buyer is entitled to delivery of the goods in accordance with the terms of the contract of sale. The rules as to delivery are—

(1) Whether it is for the buyer to take possession of the goods or for the seller to send them to the buyer is a question depending in each case on the terms of the contract. Apart from any contract, the place for delivery is the *seller's place of business*, if he has one, and, if not, his residence. But if the contract is for the sale of specific goods which, to the knowledge of the parties when the contract is made, are in some other place, that place is the place of delivery.

(2) Where, under the terms of the contract, the seller is bound to send the goods to the buyer, but no time is fixed, the seller must send them within a reasonable time.

(3) Where the goods at the time of sale are in the possession of a third person, there is no delivery by the seller to the buyer unless and until such third person acknowledges to the buyer that he holds the goods on his behalf.

(4) Demand or tender of delivery may be treated as ineffectual unless made at a reasonable hour, what is a reasonable hour



being a question of fact. For example, 6 p.m. would be considered an unreasonable hour at which to tender goods to a warehouse.

(5) Unless otherwise agreed, the expenses of putting the goods into a deliverable state must be borne by the seller. If the goods sold are delivered not to the buyer directly, but to some carrier, the rules are—

(a) Where the seller is authorised to send the goods to the buyer, delivery of the goods to a carrier, whether named by the buyer or not, for the purpose of transmission to the buyer is deemed to be a delivery of the goods to the buyer.

(b) Unless otherwise authorised by the buyer, the seller must make such contract with the carrier on behalf of the buyer as may be reasonable, having regard to the nature of the goods and the other circumstances of the case. If he omits to do so, and the goods are lost or damaged in course of transit, the buyer may either—

(i) Decline to treat the delivery to the carrier as a delivery to himself ; or

(ii) May hold the seller responsible in damages.

Unless otherwise agreed, where goods are sent by the seller to the buyer by a route involving **sea transit** under circumstances in which it is usual to insure, the seller must give such notice to the buyer as may enable him to insure the goods during their sea transit, and if the seller fails to do so, the goods are deemed to be at the seller's risk during the sea transit.

Where the seller of goods agrees to deliver them at his own risk at a place other than that of the place where they are when sold, the buyer must, unless otherwise agreed, take any risk of deterioration of the goods necessarily incident to the goods during the course of transit.

**CONDITIONS AND WARRANTIES.**—The buyer is entitled to have any conditions and warranties relating to the goods duly observed and performed.

A **Warranty** means any stipulation with reference to the goods which are the subject of a contract of sale, but collateral to the main purpose of such contract, the breach of which gives rise to a claim for damages but not to a right to reject the goods and treat the contract as repudiated.



A **Condition** is a similar stipulation which is an essential term of a contract, so that it goes to the root of the contract and the breach of which may, therefore, give rise to a right to treat the contract as repudiated. Whether any particular stipulation in a contract of sale is a condition or warranty depends in each case upon the construction of the contract, but—

(1) It may be a condition although called a warranty in the contract.

(2) Unless a different intention appears, stipulations as to time of payment are not deemed to be of the essence of a contract of sale, but whether any other stipulation as to time is of the essence of the contract or not depends upon the terms of the contract.

The general rule of English law is expressed in the maxim *caveat emptor* (i.e. let the buyer beware); hence, in the absence of any expressed stipulation by the buyer, the law will not imply any conditions or warranties in favour of the buyer except those mentioned below.

In every contract of sale, unless the terms of the contract are such as to show a different intention, there is—

(a) An implied condition on the part of the seller that, in the case of a sale, he has a right to sell the goods, and that, in the case of an agreement to sell, he will have the right to sell the goods at the time when the property is to pass.

(b) An implied warranty that the buyer shall have and enjoy quiet possession of the goods.

(c) An implied warranty that the goods shall be free from any charge or encumbrance of a third party not declared or known to the buyer at the time when the contract is made.

**RIGHTS OF THE SELLER.**—Rights against the Buyer. The seller has the right to require the buyer—

(1) To accept the goods; and

(2) To pay for the goods,

in accordance with the terms of the contract of sale.

The buyer is deemed to have accepted the goods—

(1) When he intimates to the seller that he has accepted them;

(2) When the goods have been delivered to him and he does any act in relation to them which is inconsistent with the ownership of the seller (e.g. if he re-sells them); or



(3) When, after the lapse of a reasonable time, he retains the goods without intimating to the seller that he has rejected them.

Unless otherwise agreed, when goods are delivered to the buyer and he refuses to accept them, having the right to do so, he is not bound to return them to the seller, but it is sufficient if he intimates to the seller that he refuses to accept them. When the seller is willing and ready to deliver the goods and requests the buyer to take delivery, and the buyer does not, within a reasonable time after such request, take delivery, he is liable to the seller—

(1) For any loss occasioned by his neglect or refusal to take delivery ; and

(2) For a reasonable charge for the care and custody of the goods.

In all cases unless otherwise agreed, delivery of the goods and payment of the price are concurrent conditions ; that is to say, the seller must be ready and willing to give possession of the goods to the buyer in exchange for the price, and the buyer must be ready and willing to pay the price in exchange for the goods.

**Rights against the Goods.** Notwithstanding that the property in the goods may have passed to the buyer, an unpaid seller has by implication of law—

(a) A lien on the goods for the price while he is in possession of them ;

(b) In case of the insolvency of the buyer, a right of stopping the goods in transit after he has parted with the possession of them ; and

(c) A right under certain conditions to re-sell the goods.

Where the property in the goods has not passed to the buyer, the unpaid seller has a right of withholding delivery, similar to and co-extensive with his rights of lien and stoppage *in transitu* in cases where the property has passed to the buyer.

A seller of goods in this connection includes any person who is in the position of a seller (e.g. an agent of the seller to whom the bill of lading has been endorsed, or a consignor or agent who is himself paid or is directly responsible for the price). A seller is deemed to be unpaid—

(a) When the whole of the price has not been paid or tendered, and



(b) When a bill of exchange or other negotiable instrument has been received as conditional payment and the condition on which it has been received has not been fulfilled by reason of the dishonour of the instrument or otherwise.

**The Unpaid Seller's Lien.** The unpaid seller who is in possession of the goods is entitled to retain possession of them until payment or tender of the price—

(a) Where the goods have been sold without any stipulation as to credit ;

(b) Where the goods have been sold on credit but the term of credit has expired ; and

(c) Where the buyer becomes insolvent ; that is to say, where he has either ceased to pay his debts in the ordinary course of business or cannot pay his debts as they become due, whether he has committed an act of bankruptcy or not.

The unpaid seller loses his lien thereon—

(1) When he delivers the goods to a carrier for the purpose of transmission to the buyer without reserving the right of disposal of the goods ;

(2) When the buyer lawfully obtains possession of the goods ; and

(3) By waiver of the lien.

**Stoppage “in transitu.”** If and when the buyer of goods becomes insolvent, the unpaid seller who has parted with the possession of the goods has the right of stopping them *in transitu* ; that is to say, he may resume possession of the goods so long as they are in course of transit, and may retain them until payment or tender of the price.

The right may be exercised either—

(1) By the seller taking actual possession of the goods ; or

(2) By his giving notice of his claim to the carrier in whose possession the goods are.

Such notice may be given either to the person in actual possession of the goods or to his principal, but in the latter case, the notice, to be effectual, must be given at such time and under such circumstances that the principal, by the exercise of reasonable diligence, may communicate it to the buyer. When notice is given to the carrier, he must deliver the goods to or according to the directions of the seller, but the expenses of such re-delivery must be borne by the seller.



The right of stoppage *in transitu* can only be exercised so long as the goods are in the course of transit, and the rules for determining the duration of transit are—

(1) Goods are deemed to be in course of transit from the time when they are delivered to a carrier for the purpose of transmission to the buyer until the buyer takes delivery of them from the carrier.

(2) If the buyer obtains delivery of the goods before their arrival at the appointed destination, the transit is at an end.

(3) If after the arrival of the goods at the appointed destination, the carrier acknowledges to the buyer that he holds the goods on his behalf and continues in possession of them as bailee for the buyer, the transit is at an end, and it is immaterial that a further destination for the goods may have been indicated by the buyer.

(4) If the goods are rejected by the buyer and the carrier continues in possession of them, the transit is not deemed to be at an end if the seller has refused to receive them back.

(5) When goods are delivered to a ship chartered by the buyer, it is a question depending on the circumstances of the particular case whether they are in the possession of the master of the ship as a carrier or as agent for the buyer. The test is whether the master is the servant of the owner of the ship or of the charterer.

(6) Where the carrier wrongfully refuses to deliver the goods to the buyer, the transit is deemed to be at an end.

(7) Where part delivery of the goods has been made to the buyer, the remainder of the goods may be stopped *in transitu*, unless the part delivery has been made under such circumstances as to show an agreement to give up possession of the whole of the goods.

With regard to the persons against whom the right of stoppage *in transitu* can be exercised, the general rule is that a second buyer of goods cannot stand in any better position than the original buyer; hence the unpaid vendor's right of stoppage *in transitu* is not, as a rule, affected by any sale or other disposition of the goods which the buyer may have made unless the seller has assented thereto. But there is one exception which is important—that where a document of title of goods (e.g. a bill of lading) has been lawfully transferred to any person as buyer or owner of the goods and that person transfers the document to another person, who takes the document in good faith and for value, and then—

(1) If such last-mentioned transfer was by way of sale, the unpaid seller's right of stoppage *in transitu* is defeated; and

(2) If such last-mentioned transfer was by way of pledge or other disposition for value, the unpaid seller's right of stoppage *in transitu* can only be exercised subject to the rights of the transferee.

**Re-Sale of Goods by an Unpaid Seller.** A contract of sale is not rescinded by a mere exercise by an unpaid seller of his right of lien or stoppage *in transitu*. If an unpaid seller has exercised the right, and he re-sells the goods, the new buyer acquires a good title thereto as against the original buyer who is in default. There are, however, three cases in which the unpaid seller has a right to re-sell, viz.—

(1) Where the goods are of a perishable nature.

(2) Where he gives notice to the buyer of his intention to re-sell, and the buyer does not within a reasonable time pay or tender the price.



(3) Where he expressly reserves a right of re-sale in case the buyer should make default.

In cases (1) and (2) the unpaid seller may re-sell the goods and recover from the original buyer damages for any loss occasioned by any breach of contract ; and in case (3), if, upon the buyer making default, the unpaid seller re-sells the goods, the original contract of sale is thereby rescinded, but without prejudice to any claim the seller may have for damages.

**ACTIONS FOR BREACH OF CONTRACT.—Remedies of the Seller.** Where, under a contract of sale, the property in the goods has passed to the buyer and the buyer wrongfully neglects or refuses to pay for the goods according to the terms of the contract, the seller may maintain an action for the price of the goods.

Where the buyer wrongfully refuses or neglects to accept and pay for the goods, the seller may maintain an action against him for damages for non-acceptance. The measure of damages in an action for non-acceptance is the estimated loss to the seller directly and naturally resulting in the ordinary course of events from the buyer's breach of contract. Where there is an available market for the goods in question, the measure of damages is *prima facie* to be ascertained by the difference between the contract price and the market or current price either—

(a) At the time or times when the goods ought to have been accepted ; or

(b) If no time was fixed for acceptance, then at the time of the refusal to accept.

In addition, the seller is entitled to recover special damages in any case where by law special damages may be recoverable. That is to say, if the contract was entered into with knowledge on the part of both seller and buyer that there were special circumstances attaching to it which in the ordinary course of things would produce special loss if the contract were broken, the buyer is liable to pay damages for such special loss.

**Remedies of the Buyer.** Where the seller wrongfully neglects or refuses to deliver the goods to the buyer, the buyer may maintain an action against the seller for damages for non-delivery.

In any action for breach of contract to deliver specific or ascertained goods, the Court may direct that the contract shall be



performed specifically, without giving the seller the option of retaining the goods on payment of damages.

Where there is either a breach of warranty by the seller, or where the buyer elects or is compelled to treat any breach of a condition on the part of the seller as a breach of warranty, the buyer is not by reason only of such breach of warranty entitled to reject the goods, but—

(1) He may set up against the seller the breach of warranty in diminution or extinction of the price ; or

(2) He can maintain an action against the seller for damages for the breach of warranty. The measure of damages to which the buyer is entitled is the estimated loss directly and naturally resulting in the ordinary course of events from the seller's breach of contract or warranty, and he may also recover special damages in any case where they are recoverable by law. In particular—

(a) Where there is an available market for the goods in question, the measure of damages is *prima facie* to be ascertained by the difference between the contract price and the market or current price of the goods at the time or times when they ought to have been delivered ; or

(b) If no time is fixed, at the time of the refusal to deliver.

In the case of breach of warranty of quality, the loss to the buyer is *prima facie* the difference between the value of goods at the time of delivery to the buyer and the value they would have had if they had answered to the warranty.

**Sales by Auction.** Where a sale of goods takes place by auction as opposed to private treaty, the rules are—

(1) When the goods are put up by auction in lots each lot is *prima facie* deemed to be the subject of a separate contract of sale.

(2) A sale by auction is complete when the auctioneer announces its completion by the fall of the hammer or any other customary manner. Until such announcement is made, any bidder may retract his bid.

(3) Where a sale by auction is not notified to be subject to a right to bid on the part of the seller it is not lawful either (a) for the seller to bid himself or to employ any person to bid at such sale ; or (b) for the auctioneer knowingly to take any bid from the seller or any such person, and any bid in contravention of this rule may be treated as fraudulent.

(4) A sale by auction may be notified to be subject to a *reserve* or *upset* price.

(5) A right to bid may be reserved expressly by or on behalf of the seller, and where a right to bid is so reserved, but not otherwise, the seller or any one person on his behalf may bid at the auction.

(6) The capacity of the parties to a contract of sale is regulated by the general law concerning capacity to contract and to transfer and acquire property, with this additional proviso, namely—



That where necessities are sold and delivered (a) to an infant (that is, any person under 21 years) or (b) to a person who, by reason of mental incapacity or drunkenness is incompetent to contract, he must pay a reasonable price for them. Necessaries in this connection mean goods which are suitable both to the condition in life of such infant or other person, and to his actual requirements at the time of the sale and delivery.

**SALES ON THE INSTALMENT SYSTEM.**—Instalment credit is most usually and most fittingly applied to purchases of merchandise which are made by individual consumers at relatively infrequent intervals, on account of the durable character of the goods and their high cost. From this we get the consequence that the amount of consumer credit involved is unusually large and that a proportion of it is outstanding for a long period. Thus the risks, and consequently the costs, of the system are higher than in the case of ordinary short-term credit, so that conditions have to be inserted in the contract and precautions taken to safeguard the positions of the grantor of the credit and often of the buyer as well. There are risks of losses through granting credit to unsuitable persons, though these arise equally in the case of ordinary credit; and on account of the amounts involved in instalment transactions, greater precautions are likely to be taken. The seller can protect himself against such risks only by arranging a suitable relationship between the rate of payment and the value of the article so that the "re-possession" value is sufficient to compensate him for unexpected loss. At the same time, the buyer may protect himself, where possible, from complete loss of what he has already paid by being allowed to retain some proportion of the goods, as in the case of furniture sales.

There are two main types of instalment credit, namely—

- (1) A Hire Purchase contract, and
- (2) A Sale on Deferred Payment terms.

The Hire Purchase sale is a form of trade in which credit is granted to the customer on the security of a lien on the goods sold. Under such an agreement the customer takes possession of the goods at once and agrees to pay a certain sum at stated intervals. But although the goods actually come into his possession, the ownership still remains with the seller till the last instalment has been paid. On the other hand, under the system of Deferred Payments the goods become the actual property of the buyer on the payment of the first deposit, and the seller has no right to retake possession of



them if the customer fails to pay his instalments, and can only sue for the amount due.

In undertaking business on the hire purchase plan, the trader should observe certain precautions—

(1) Care should be taken in selecting the class of customers with whom sales on the hire purchase system are made, otherwise extensive losses through default may occur.

(2) The period of repayment should be adjusted so that the whole value of the property is paid before it becomes worn out.

(3) The property concerned should be such that it is easy to retake possession in the event of default.

The instalment system, although convenient to trader and customer alike, possesses certain drawbacks—

(1) People may be tempted by the instalment plan to buy things which they cannot afford.

(2) It adds considerably to the price of the goods, since allowance must be made for the cost of interest and collection of instalments as well as for losses due to the defaults of customers.

(3) The fact that the trader has the right to reclaim goods under a hire purchase contract does not protect him completely from the risk of heavy loss, for the goods when reclaimed are secondhand and often of little value.

Prior to the passing of the *Hire Purchase Act, 1938*, the seller under a hire purchase agreement could retake possession of the whole of the goods sold to a defaulting customer, as well as keep by way of forfeit all the instalments which had been paid. The Act seeks to remedy this and other abuses by providing that, in case of non-payment of instalments by the buyer, the seller can no longer take the goods away against the hirer's will, but must bring the matter before the County Court. The court, after considering all the facts, will decide what is to be done. Should the seller seize the goods, contrary to the provisions of the Act, then the customer can recover from him all the payments that have been made. The *Hire Purchase Act, 1938*, further provides—

(1) That the seller must furnish the customer with a copy of the hire purchase agreement, and before this agreement is signed the customer must be informed of the cash price of the goods in question as well as of their instalment price.

(2) Where the buyer moves and takes the goods with him, he must acquaint the seller with his new address.

The instalment agreement should be carefully studied by the buyer in order to determine whether what is intended is an out-and-out sale with payment by instalments or a true hiring agreement with an option to purchase.



## TEST PAPER XXIV

1. Name the principal factors to be borne in mind by the trader when making his purchases.

2. Under what circumstances may the trader reject, on delivery, the goods which have been ordered by him?

3. Mention some of the methods by which the trader usually indicates the quality of the goods which he desires to purchase.

4. Where a seller sells goods in the course of his business to a buyer whom he knows to be buying for a special purpose, what special obligation, if any, is imposed on the seller?

5. What conditions are implied in a contract for the sale of goods—

(a) by description; and

(b) by sample and description?

A is shown a handkerchief which he is told is an "Irish linen handkerchief." A thereupon orders a dozen equal to sample. After they are delivered, A discovers that they are not real Irish linen, but that they are in every respect equal to the sample which he inspected. What is the position of A?

6. Explain how goods are sold according to analysis?

7. Give an illustration to show the requirements of a contract of sale.

8. Distinguish *sale from agreement to sell*, and explain why the distinction may be important.

9. Explain the meaning attached to the following terms—

Barter; Sale; Gift.

10. What is the legal meaning of the term "Goods"?

11. Classify the kinds of goods which may form the subject of a contract of sale.

12. Is it necessary for a contract of sale to be in writing?

13. What are the provisions of Section 4 of the Sale of Goods Act, 1893?

14. Where a memorandum of a Contract of Sale is required, what must the memorandum contain?

15. By what principles should the small shopkeeper be guided in his buying? When effecting his purchases, what factors must be taken into consideration besides the mere price per unit?

16. In a contract for the sale of goods, what rules determine at what time the property in the goods passes?

17. Distinguish between a "Warranty" and a "Condition."

18. "In contracts for the sale of goods, the general rule is *caveat emptor*." Comment on this statement, indicating any limitations or exceptions to the universal applicability of the rule.

19. What title does a buyer, as a general rule, acquire to the goods he purchases?

20. What rights has the seller against the buyer under a Contract of Sale?

21. What rights are, or may be possessed by an unpaid vendor of goods?

22. Explain the nature and effect of the right of *stoppage in transitu*. Under what circumstances, and by whom, can it be exercised?

23. How may the right to stop goods *in transitu* be lost?

24. When has an unpaid seller a right to re-sell the goods which are the subject-matter of a contract of sale?

25. What are the rights of a buyer where the seller refuses to deliver goods in which the property has passed?

26. A buyer purchases goods subject to a warranty of soundness, which is subsequently shown to be unfulfilled. What is the position of the buyer, assuming that he has paid for and taken delivery of the goods?

27. Distinguish the system of hire purchase from that of deferred payments. In what respect does the Hire Purchase Act, 1938, affect these methods of doing business?

28. Consider the hire purchase system from the standpoint of the buyer. Is this type of trade likely to extend? Give reasons for your answer.



## CHAPTER XXV

### ORGANISATION OF THE RETAIL TRADE

**NATURE OF THE RETAIL TRADE.**—We have defined trade as the means whereby the personal hindrance in the exchange of commodities is overcome. Under modern conditions of specialisation, however, the intervention of a number of specialist agencies is usually called for in the passage of goods from the producer to the final consumer, the last of these being the retail trader. Hence we may define the retailer as a trading intermediary engaged in the distribution of consumers' goods who is in direct contact with the ultimate consumer. In the words of the Linlithgow Committee, "The business of retailing consists in the sale to consumers of a wide variety of products which are assembled at the retailer's premises for that purpose, sufficient in variety and quantity to meet the requirements of a large number of individual households."

On the basis of these definitions we may briefly consider the particular economic functions performed by the retail trader. These may be enumerated as follows—

(1) **Holding Stocks.** The retailer holds stocks of goods ready for immediate use which he is prepared to sell in small quantities. The single household is not in a position to store large quantities of every article which comes into daily use, since this would necessitate an outlay which the majority of consumers could not face. Again, the storage facilities of the average house are limited so that purchases must be limited on this ground also. This factor appears to have been accentuated in recent years on account of the severe limitation of space in the modern "labour saving" house. Finally, as many consumable goods are of the perishable type, storage for any period of time demands special facilities, and here again, the consumer must buy in small quantities for immediate consumption. These difficulties are overcome for him by the existence of the retailer who holds stocks of goods in a shop located as near as possible to potential consumers, so that they are put to the minimum of trouble and inconvenience in satisfying their requirements.

(2) **Providing Variety of Choice.** Under modern conditions of



production the majority of consumers' goods can be obtained in considerable variety, and consumers tend to differ considerably in their preferences. Here again the retailer sets himself to meet consumer demand by assembling in his shop an assortment of goods—the products of different manufacturers—so that his clients may select what they require. Were it not for the existence of the retailer, the consumer would scarcely be able to exercise this right of choice to the extent which is now possible. Since the War, the retailer's difficulties in this respect have increased considerably, since the demands of consumers for variety in the goods which they purchase have been greatly accentuated. The result has been that retailers have had to buy more cautiously and in smaller quantities, whilst at the same time they incur greater risk of loss through being left with stocks of unwanted goods on their hands. These circumstances all tend to increase the costs of retail distribution.

**(3) Supplying Information to the Public.** As civilisation advances men's wants increase in number and diversity with the result that production is correspondingly stimulated to meet them. Were there not some agency in existence through the medium of which goods can be displayed and demonstrated, the consumer would remain unaware of the existence of large classes of new merchandise. Again the retailer performs the service of drawing the attention of the consumer to these new goods and stimulates sales by offering facilities for their inspection. The value of this service is especially evident in the sale of such merchandise as textile fabrics, clothing or furniture.

**(4) Expert Advice.** Closely allied with the foregoing service is the advice which the efficient retailer can give to his clients with regard to their purchases. The retailer, by virtue of his training and experience, should be an expert in the class of goods which he handles and, as such, is competent to advise his customers. Were the latter compelled to deal direct with the producer, they would be likely to suffer inconvenience and loss on account of their lack of knowledge of what they were buying. The retailer can make good this deficiency and, indeed, must do so, since the continuance of his relationships with his customers depends in considerable measure upon his success in performing this service. He also frequently gives advice after the sale has been made, as in the case of dealers in photographic supplies.



(5) **Outlet for Producers.** In addition to his services to the consumer, the retailer performs a valuable service to the producer by providing him with an outlet for his goods. The manufacturer is thus relieved of the detail work connected with distribution, and can concentrate upon production and market his product through the usual trade channels in bulk. The work of making individual sales to consumers in small quantities thus devolves upon the retailer, the separation of functions being usually conducive to greater efficiency.

(6) **Miscellaneous Services.** In addition to the foregoing, the retailer renders a wide and ever-growing range of services to the consumer. These may include free delivery of goods to customers scattered over a wide urban and suburban area. Again, extensive service may be performed by calling for orders in the better class residential districts. Credit dealing on weekly or monthly terms is another conspicuous feature of many branches of the retail trade. All of these services are sought by consumers even though they add very considerably to the already heavy costs of retail distribution.

**TYPES OF RETAIL ORGANISATION.**—The services which we have just examined are by no means all performed by every type of retailing organisation. Indeed, a survey of the field of retail distribution reveals the existence of organisations of widely varying types and of even more widely varying degrees of efficiency. Before proceeding further we must therefore examine the general structure of the retail trade, and attempt some classification of the various elements which compose it. In the first place, we may draw a line of demarcation between the *itinerant* and the *fixed* forms of retail trade, that is, between those traders who conduct their business from vehicles which they bring to the doors of their customers, and those who carry on trade from definite business premises. Considering the second class, i.e. the fixed retail trade, we may distinguish between small-scale and large-scale organisations. It must be admitted that this mode of division does not offer a watertight classification, but it offers a convenient basis for examination.

(1) **Itinerant Traders.** Under this heading we may include a variety of dealers, such as pedlars and hawkers, market traders and cheap jacks whose common characteristic is that they usually have no fixed premises and very little stock, so that they can operate on a minimum of capital outlay. Such traders are found dealing in



fruit, vegetables, and fish, and may operate as regular dealers all the year round or purely casually during a season. This type of trading is viewed with considerable disfavour by established shopkeepers who consider that such traders offer unfair competition inasmuch as they make little or no contribution to local rates. The demand has been made that local authorities should regulate hawkers and make them take out a local licence in addition to the licence fee payable to the State under the Hawkers Act, 1888. Some local authorities already have the power under the local Acts to license and regulate hawkers. Although this question of itinerant trading creates certain problems, such dealers give valuable service to consumers in keeping down prices, whilst they render a service to producers in clearing the market of surplus produce which would otherwise deteriorate and be wasted.

In the case of the milk trade, we have a type of business which may be regarded as transitional between itinerant and fixed retailing. There exists a class of milk pedlars who may fitly be described as itinerant traders since they have no premises of their own, but may, for a fee, obtain such services as they require from another dealer, such as facilities for cleansing utensils and storage. The majority of milk vendors, however, have premises of their own, at which they can treat the milk and possibly sell it over the counter. The possession of such premises serves to take them out of the itinerant class strictly speaking, though inasmuch as the bulk of their sales are made from door to door they have much in common. Of a similar character is the distribution of ice cream where a central factory sends roundsmen into different districts.

Under this heading, too, we may note what is termed the "Club" system under which large quantities of clothing, boots and shoes and miscellaneous articles are bought in working-class districts in many areas. Shops send out agents who persuade people to take tickets which are paid for by weekly instalments. Thus, a person taking a ticket valued £1 would pay for it by twenty-one weekly instalments of 1s. After making the first payment, the customer can go to the shop and choose what he requires up to the value of the ticket. The shop does not recognise the customers, but deals with the agent, who becomes responsible for the collection of the money.

(2) **Small-scale Fixed Retail Trade.** Under this heading we must



# ESTIMATED NUMBER OF DIFFERENT TYPES OF RETAIL SHOPS IN GREAT BRITAIN

## TYPES OF RETAIL SHOPS

<i>Type of Shop</i>	<i>Number of Shops or Branches</i>	<i>Aggregate Annual Turnover</i>	<i>Average Annual Turnover per Shop or Branch</i>
Single Shops	585,000	£1,000,000,000	Under £2,100
Multiple Shops	30,000	£300,000,000	£10,000
Departmental Stores	1,000	£150,000,000	£150,000
Co-operative Distributive Societies	10,000	£200,000,000	£20,000



place all traders who conduct their business from a properly-established shop, but whose turnover is restricted to a relatively small amount. A striking feature of the modern distributive system is the large number of small establishments engaged in the retail trade. Although no exact figures are available it is estimated that the number of shops in England and Wales exceeds 600,000. Of these, sample inquiries in Birmingham, Leeds, and Sheffield suggest that anything from one-half to two-thirds are of the "family" type, i.e. they employ no assistants outside the shopkeeper's family and do an average trade of £10 a day. In this connection, too, the Linlithgow Committee pointed out that in the baking trade, even in the large cities, there are many bakers who handle less than ten sacks of flour a week, while the number of meat traders who do no butchering, but buy their meat in small quantities in the wholesale market is considerable.

The reason for the prevalence of the small retail business is not far to seek. It is possible to establish such a business with a very small capital outlay either by converting the front room of an ordinary house into a shop, or by renting a small shop with the private residence attached. In such circumstances, the rent of the premises may come to little more than the rent of a private dwelling-house. Expenditure on fittings and fixtures can be reduced to a minimum, whilst stock can usually be obtained from a wholesale house on favourable credit terms. Finally the proprietor enlists the services of his wife and family for the purpose of running the business, thereby saving the payment of wages to assistants. Indeed, he himself may continue to work at some other occupation and treat the shop as a spare time employment designed merely to supplement his income.

Such a business comes into existence very easily and, it may be added, disappears easily and frequently, only to be replaced by new ventures. A large number of these concerns are, moreover, highly inefficient. It may be argued that the existence of so many sources of supply sets up keen competition, leading to a reduction of selling prices to the consumer. Yet, a large proportion of such establishments work under the disability of excessive costs which render them powerless to provide the real and effective competition capable of reducing profit margins. The average small shopkeeper has not, and cannot hope to create, a sufficient turnover to yield



him a satisfactory income without charging his customers, directly or indirectly, more than his services are worth. Again, many of the services which we have enumerated as being rendered by the retailer are performed only indifferently by traders of this class. Usually such dealers have neither technical knowledge of the goods they sell nor the business knowledge necessary to give any hope of success. In consequence their inefficiency is manifest in every branch of their activity. The small retailer has a function, and a very valuable one, to perform in the field of distribution, but the existence of widespread inefficiency acts as a barrier to progress.

(3) **Large-scale Fixed Retail Trade.** In contrast with the small-scale retail undertaking we have those which characteristically conduct their operations on a large scale. In their origins, these large retailing businesses usually spring from the small types which we have just considered, and the form which they have taken is very largely dictated by external economic conditions. It may be, for example, that a retailer dealing in one line of goods, such as drapery, finds that he can attract a large number of customers for that particular class of merchandise. In order to increase his turnover he decides to add another class of goods and opens a new department for this purpose. In this way we have the evolution of the *Departmental Store* which, in its developed form, brings together in one building a large number of consumers' goods classified on the basis of department. Retail expansion may, however, take another form. The trader dealing in a single line of goods who finds his turnover expanding may be unwilling to add new lines of goods to stimulate business further, but prefer to develop the existing business. If he confines his business to one building there will be a limit to his increase of turnover, and in order to overcome this difficulty, he opens branches in selected districts, stocking the same lines of goods as the parent shop. In this way we get the development of the *Multiple Shop* or *Chain Store* systems, i.e. the type of business handling a limited range of goods but selling through a large number of retail outlets.

Combining the features of these two types we have the chain of departmental stores which, however, is not nearly so popular in this country as in Canada. A well-known example of this type of business is given by Lewis's, Ltd., who operate large departmental stores of a single type in Liverpool, Manchester, Birmingham,



Glasgow and Leeds. Selfridge's Provincial Stores and the Drapery Trust are other examples of a somewhat similar tendency. Another variation is what is known as the *Fixed Price Chain Store*, i.e. a multiple shop system selling a wide range of articles with a low maximum price above which no articles are sold. In this country, this type of organisation is represented notably by Woolworth's, with their maximum price of 6d., or Marks and Spencer's with a 5s. maximum.

On an entirely different basis we have retailing organisations controlled by consumers themselves in the *Co-operative Retail Societies*. These organisations differ from those previously mentioned not so much in external organisation or internal administration as in control and direction. The "capitalistic" undertaking represented by the foregoing types is controlled by managers and directors who are responsible to the shareholders who are the real owners of the business, and who take the profits which result from its operations. On the other hand, the co-operative undertaking is controlled by managers and directors who are appointed by and responsible to the members, who are themselves the customers of the undertaking. In these organisations, over 98 per cent of the total trade done is with customers who are members and therefore part-owners of the organisation. The surplus resulting from such trading is distributed amongst members in proportion to their purchases.

\* A further type of retail organisation which is usually considered to be of the large-scale type is the *Mail Order business*. In this case we have a type of business where the "personal" contact between the seller and his potential customer is made through some form of advertisement—usually press advertising supported by direct mail. Since the customer cannot visit the business premises and make a personal examination of the goods, considerable expenditure has to be incurred in the preparation of the descriptive advertising literature, which, in most cases, must be carefully illustrated. The classes of goods which can be sold by this method are restricted to those which are relatively valuable in proportion to their weight, for, as the most convenient method of delivery is the parcels post, goods which are heavy in proportion to their value will not stand the cost of carriage. The mail order business is of value in bringing a wide choice of goods before customers who are precluded by reason of



distance from visiting big shopping centres. In this country, however, owing to the fact that few people are at any great distance from a shopping centre, the business has not developed to the same extent as in the United States. There are few examples of the "pure" mail order business in this country, and the most successful appear to be carried on as a special department of the departmental stores. Even in the United States the introduction of the cheap car, which has increased the mobility of the inhabitants of the rural areas, has caused a set-back in the fortunes of the mail order houses and has caused many of them to go into the departmental store business.

**THE SMALL SHOP.**—In our survey of the general structure of the British distributive system we have already commented upon the fact that the small family shop is the predominant type of trading unit. These small shops are of two general classes. There is, first of all, what we may term the *General Shop*, that is, a shop of the general utility type whose proprietor does not restrict his stocks to any particular line of goods but stocks whatever his experience has told him that his customers are likely to require. There are obvious limits to which such diversification of stocks can be carried, but the usual class of goods is the consumers' goods which are in every day domestic use and where patronage may be secured on account of convenience. This is especially the case with branded goods where, assuming proper conditions of storage, quality and price are the same wherever purchases are made. The second type of small shop is what has been termed the *Specialty Shop* where specialisation on one line of goods takes place. Such shops as these are found in the established shopping centres rather than scattered amongst dwelling houses as are those of the first class. Thus we may have shops concentrating on the sale of millinery, men's or women's wear, jewellery, boots and shoes, or furniture. In the case of such shops as these, the proprietor usually relies upon his special knowledge of the goods to give such service to his customers as to compensate them for the higher prices which he is compelled to charge. Here again he frequently differs from the proprietor of the first class of shop, whose knowledge of the goods he sells is frequently very poor.

The question of the survival of the small retailer in the face of the competition offered by large-scale retailing organisations is one which has often been debated. In the first place, as we have already



seen, the ease with which the small shop of the "general" type can be established is likely to militate against any great reduction in numbers. Again, the convenience which the small shop can offer to the consumer buying from hand to mouth is yet another factor working for its survival. Furthermore, we have to take into consideration the factor of the personal contact between shopkeeper and customer which is much more easily achieved and productive of better results in the small shop than in the large organisation. There is a certain degree of "consumer snobbishness" which is gratified by the personal attention of the small shopkeeper and his knowledge of personal idiosyncrasies.

**THE RETAILER'S STATISTICS.**—In order that the retailer may exercise effective control over his business, it is essential that he shall keep systematic records of all business transactions. The starting point of these records is, of course, the financial accounts which, in order to be of the greatest possible value, should be kept on double-entry principles. These records may be made to yield much valuable information on such matters as the following—

(1) The total liabilities of the business to trade suppliers and others, together with the amount owing to each individual.

(2) The total amount due to the business from debtors and the amounts due from individuals, together with the period of time for which each account has been outstanding. This information is of considerable importance in forming decisions with regard to the granting of new credit.

(3) The turnover of the business and the expenses incurred in making that turnover.

(4) The various items of property held by the business in the form of fixed and circulating capital, together with a statement of the trader's capital account.

The information obtained on the basis of these accounts will in all probability be sufficient to meet the needs of the small retailer. As the business increases in size, however, more detailed information becomes essential for the effective administration of the business. When the undertaking comprises a large number of departments or branches, highly complex problems of financial control arise, and at this stage statistical control must be employed to supplement the information yielded by the financial books. It may be emphasised that these latter still form the basis of the greater part of the



# The

## RETAILER'S ACCOUNTS

Kept on Double Entry Principles are found in

### DAY BOOKS

(a record made as the Transactions Occur)

#### Purchases Book

Entered up from Invoices as received from Suppliers after Checking.

#### Sales Book

Entered up from Vouchers made out by the Salesmen in the Shop.

#### Returns Books

Entered up from the Debit or Credit Notes Issued and Received.

#### Cash Book

Entered up by Cashier when Cash is Received or Paid.

### LEDGERS

(a classified record of Personal Accounts, Property Accounts, Income and Expense Accounts)

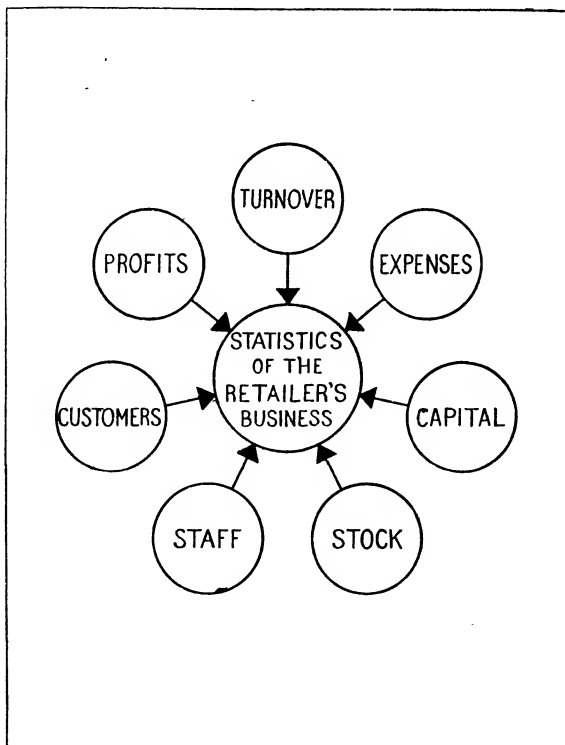
Entered up by Ledger Clerk in the Office from the Day Books in order to show

- (a) Accounts Owning to the Business.
- (b) Amounts Owed by the Business.
- (c) Expenses of Selling.
- (d) Turnover and Takings.
- (e) Capital of the Proprietors.
- (f) Profit Earned.



business statistics, but the aim of the statistical method is to show clearly the causal relationships which exist between the various parts of the undertaking. The financial records, which deal with many of the figures in bulk, are analysed in detail in order to reveal latent tendencies. On the basis of such analyses, graphs and charts may be prepared to illustrate such matters as the relation of the purchases to the selling price, the ratio of expenses to sales, the ratio of profit to capital invested, and so on. By the use of such devices the data relevant to a particular business problem may be more readily grasped by those responsible for business administration.

### BASIS OF THE RETAILER'S STATISTICS



The chief accounting figures utilised in the compilation of the retailer's statistics are shown in the diagram above. They include the figures of turnover, expenses, the capital employed in



the business, the average stock kept in the warehouse, the number of the staff, the number of customers and the net profit. From these data, a variety of decisions may be taken affecting such matters as purchasing and advertising policies, the extension or the elimination of particular departments, and the best utilisation of staff. Amongst other things, statistical control confers the following advantages on the retailer—

(1) It gives him an accurate insight into the composition and the fluctuations of his turnover.

(2) It provides him with a detailed analysis of expenses so that he may control them effectively.

(3) He may compute, with a considerable degree of precision, the speed of stock turnover, either in bulk or in respect of particular lines.

(4) He can form a reliable estimate of the relative efficiency of the staff in the different departments or branches.

(5) Statistics compiled on a uniform plan may be employed as a basis of comparison with other undertakings in the same trade.

**Turnover.** This is one of the most important figures connected with the retailer's business since it is one of the main factors upon which net profit depends. It may be defined as the amount of the net sales of the business during a trading period. The amount of the turnover, based upon the selling prices, may be arrived at as follows—

	£	£
<b>Total Cash Sales</b> . . . . .	15,000	
<i>Less Returns and Rebates</i> . . . . .	100	
<b>Net Cash Turnover</b> . . . . .		14,900
<b>Total Credit Sales</b> . . . . .	30,000	
<i>Less Returns and Rebates</i> . . . . .	1,900	
<b>Net Credit Turnover</b> . . . . .		28,100
<b>Total Turnover</b> . . . . .		<u>£43,000</u>

These figures show the total turnover of the concern for the whole of a trading period, but in order to obtain the greatest value from them, it will probably be necessary to prepare an analytical statement showing how the turnover is distributed between the departments of the business, and also possibly over the months of the year. If only the total figures are considered, a very misleading impression may be gained. There may, for example, be a highly satisfactory increase in the total turnover, but further analysis



# TOTAL TURNOVER ANALYSED DEPARTMENTALLY

Month	All Departments			Department A			Department B			Department C		
	Cash Sales	Credit Sales	Total	Cash Sales	Credit Sales	Total	Cash Sales	Credit Sales	Total	Cash Sales	Credit Sales	Total
January	£ 2,110	£ 1,742	£ 3,852	£ 1,010	£ 890	£ 1,900	£ 780	£ 640	£ 1,420	£ 320	£ 212	£ 532
February	1,943	1,440	3,383	965	740	1,705	698	520	1,218	280	180	460
March	1,732	1,357	3,089	860	675	1,535	612	517	1,129	260	165	425
April	1,628	1,368	2,996	780	698	1,478	608	496	1,104	240	174	414
May	1,510	1,250	2,760	715	620	1,335	595	420	1,015	200	210	410
June	1,481	1,115	2,596	710	615	1,325	496	320	816	275	180	455
July	1,501	1,284	2,785	726	608	1,334	515	480	995	260	196	456
August	1,761	1,475	3,236	825	750	1,575	620	475	1,095	316	250	566
September	1,682	1,350	3,032	780	620	1,400	612	520	1,132	290	210	500
October	1,545	1,276	2,821	820	540	1,360	305	496	1,001	220	240	460
November	1,708	1,501	3,209	840	780	1,620	570	456	1,026	298	265	563
December	2,130	1,760	3,890	1,010	890	1,900	820	580	1,400	300	290	590
Total	£ 20,731	£ 16,918	£ 37,649	10,041	8,426	18,467	7,431	5,920	13,351	3,259	2,572	5,831



may show that this is due to one or two departments, and that other branches of the business are losing ground. Such a table may be constructed on the lines shown on page 285, on the supposition that the business comprises three departments. The figures of turnover, if ascertained daily or monthly, may be shown in the form of a graph which may be used to illustrate—

(1) The course of sales during the month. It would show the effect of pay days and holidays on the turnover of the business.

(2) The state of the turnover in comparison with that for the same month of the previous year.

(3) The effects of advertising campaigns and special bargain sales.

(4) The effects of unknown influences which call for further investigation, since they may arise from causes within the business which may be eliminated.

**Expenses.** In a small retail business it may be a matter of some difficulty to arrive at a correct assessment of business expenses on account of the peculiar conditions under which the concern is carried on. As we have already seen, the small retail shop is frequently conducted on a "family" basis, and the proprietor's dwelling-house and shop are often on the same premises. If the premises should be rented, it should be a fairly easy matter to apportion the rent so that a fair charge is made against the profits of the business in respect of this expense. If the proprietor owns the premises himself, he should again make an estimate of their rentable value and charge this sum against the profits. Again, if he or his family give service to the business, some allowance should be made in respect of this work, since if it were necessary to engage the services of an outside person, the expense of so doing would be chargeable against the profits.

These considerations are mainly applicable to small retail businesses and do not arise in the case of large concerns where business is conducted on a much more formal basis. In the latter case, however, the question of expense control and determination assumes formidable dimensions and becomes a problem of first-class importance. In a large concern there appears to be an inherent tendency for expenses to mount up which, unless carefully checked, must result in a serious diminution of trading profits. The first requisite of efficient expense control is a careful classification of expenses in order to secure uniformity. Accurate comparison of the expenditure

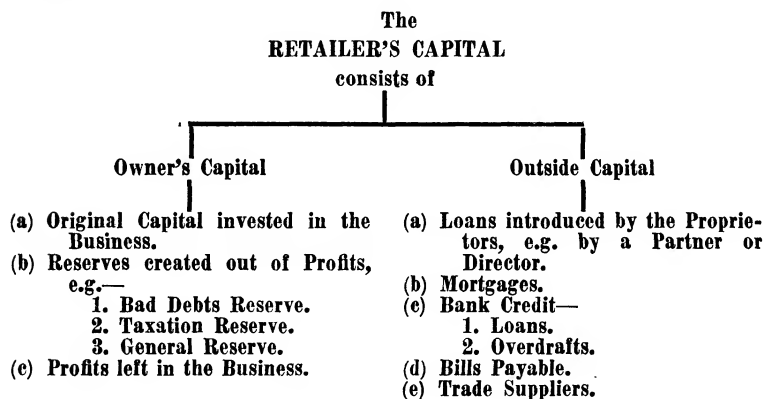


under a given heading becomes impossible if certain items are sometimes included and sometimes omitted. Thus, under the heading of "Dispatch Expenses" it may be decided to include the following items—

**Packing Materials Used**  
**Carriage**  
**Parcel Postage**  
**Motor Licences**  
**Motor Insurance**

**Garage Stores**  
**Hire of Vans**  
**Drivers' Expenses**  
**Motor Repairs**  
**Painting Vans**

In the absence of such a definite classification, "Motor Insurance" might sometimes be included in the above, and sometimes under "Insurance."



**Capital.** As shown in the accompanying diagram, the capital of a business is derived from two sources, namely, that which is supplied by the proprietors themselves, either in the form of their original investment or of undistributed profits, and that which is provided by outside persons. In the latter case, capital may be provided in a number of ways, such as by a member of a partnership firm lending money to the business as distinct from investing capital in his capacity as part proprietor. Again, money may be borrowed, with or without security from friends, or by the mortgage of property. It may also be raised by way of a loan or an overdraft from a bank, though in this case, security will in all probability be required. Finally, a very important source of outside capital is provided by trade credit, extended to the retailer by wholesalers and manufacturers. Such traders, by allowing the retailer to control and



dispose of stocks of goods for which he is expected to pay at some defined time in the future, in effect place some of their working capital at his disposal. •

The capital secured from these various sources is, of course, represented by the assets held by the business, and it is essential that close control be exercised over the composition of these assets. It must be the aim of the retailer to employ his resources in the most remunerative way possible, and yet at the same time meet his commitments as they fall due. Hence, he will have to keep a cash balance sufficient to meet the claims of trade creditors, to pay the wages and salaries of the staff, and to meet other expenses as they fall due. At the same time he must remember that cash in the till or on current account at the bank is an unremunerative asset and therefore must be restricted as far as possible. The annual accounts will, of course, give the desired information regarding the composition of the retailer's capital, but it is necessary that the position should be known with certainty at more frequent intervals, particularly in a business of any size. In order to give this information, a statement on the lines of the example shown on page 289 may be submitted to the proprietors or directors at convenient intervals—usually every month.

**Stock.** An important class of statistics is concerned with the control of stocks of goods held by the trader. These usually represent a substantial part of the retailer's working capital, and it is essential that they should be under proper control in order to reduce losses and wastage to the minimum. A knowledge of the average stocks held in a business is necessary if we wish to calculate the *speed of turnover* of stocks. We have already defined turnover as the net sales made during a trading period, and if this figure be compared with the average stock of goods at sale price, held by the dealer during the period, we can find how many times the stock has been turned over in the period in question. This forms a valuable index of the efficiency of business operations. A rough approximation of the value of the average stock at selling price may be obtained by taking the average of the opening and closing stocks for the trading period. Thus, if the stock on 1st January were £500 and that on 31st December were £600, the average stock by this method would be  $\pounds(500 + 600) \div 2 = \pounds550$ . This figure may not be very accurate since the stock at the end of a trading period may not be



**FINANCIAL STATEMENT**  
as on 30th November, 19..

	£	s.	d.	£	s.	d.
<b>1. Cash Statement—</b>						
Cash on Hand . . . . .	41	10	6			
Bank Balances—						
(a) Current Account . . . . .	1126	3	2			
(b) Deposit Account . . . . .	3678	8	6			
	£4846	2	2	£4846	2	2
<b>Total . . . . .</b>						
<b>2. Approximate Receipts for Coming Month—</b>						
(a) On Bills Receivable . . . . .				3960	—	—
(b) On Ledger Accounts . . . . .				976	—	—
(c) Other Sources . . . . .				28	—	—
<b>Total . . . . .</b>				£4964	—	—
<b>3. Commitments for Coming Month—</b>						
(a) On Bills Payable . . . . .	520	—	—			
(b) On Accounts Payable . . . . .	1210	2	6			
(c) Operating Expenses—						
(1) Wages and Salaries . . . . .	210					
(2) Rent and Rates . . . . .	130					
(3) Debenture Interest . . . . .	80					
(4) Miscellaneous . . . . .	20					
	440	—	—			
<b>Total . . . . .</b>	£2170	2	6	£2170	2	6
<b>4. Value of Stocks—</b>						
Department A . . . . .				380	—	—
" B . . . . .				960	—	—
" C . . . . .				450	—	—
" D . . . . .				280	—	—
<b>Total . . . . .</b>				£2070	—	—
<b>5. Overdue Accounts—</b>						
Wm. Buyers . . . . .				25	—	—
Owen More . . . . .				60	—	—
Sundry small a/cs. . . . .				10	—	—
<b>Total . . . . .</b>				£95	—	—

Signed John Smart,  
(Secretary)



an accurate reflex of stocks during the period. In many retail businesses, stocks will be deliberately reduced at the end of the period in order to relieve the burden of stock-taking. A more accurate method may be based on the average of the monthly figures as follows—

Total Stock on	31st January	.	.	.	.	£
"	"	28th February	.	.	.	220
"	"	31st March	.	.	.	300
"	"	30th April	.	.	.	290
"	"	31st May	.	.	.	250
"	"	30th June	.	.	.	290
"	"	31st July	.	.	.	320
"	"	31st August	.	.	.	310
"	"	30th September	.	.	.	300
"	"	31st October	.	.	.	280
"	"	30th November	.	.	.	250
"	"	31st December	.	.	.	260
						240

$$\text{Average Stock} = \frac{\text{£}3310}{12} = \text{£}275 \quad \text{£}3,310$$

Hence, if it is found that the annual turnover in this case is £8,250, then the rate of stock turnover is  $\frac{8250}{275}$  or 30 times per annum.

Information is now gradually becoming available as to what constitutes "normal" rates of stock-turn for particular trades, so that these figures offer an objective index of efficiency. Further, in the case of a departmentalised concern, comparisons may be made between departments, or of experience in different years, on the following lines—

#### TURNOVER OF STOCKS

Year Ended 31st Dec., 1934. With Comparative Figures for Last Year

Department		Sales	Average Stock at Selling Price	Stock Turn per Annum	Target for Year
		£	£		
A. Drapery	1933	1,300	240	5.42	6
	1934	1,500	255	5.88	
B. Furniture	1933	2,500	1,200	2.08	2½
	1934	3,500	1,500	2.33	
C. Grocery	1933	8,100	800	10.13	10
	1934	9,000	850	10.59	
Total	1933	11,900	2,240	5.31	5.3
	1934	14,000	2,605	5.38	



**Staff.** A large retail concern will keep careful records relating to staff matters, giving details as to the numbers employed in the various sections of the business ; for example, in the different selling departments, the workshops, the administration, and the auxiliary staff. In this way a check may be kept upon unnecessary staff expansion by transferring assistants from one section to another where this is possible. At the same time, a comparison may be made between the staffs and the turnover of each department and provision made for extra staff when the need arises. Again, statistics may be compiled with regard to the costs and results of salesmen in order to ascertain those who are worthy of promotion, and to eliminate those who cannot attain a reasonable standard. Such statistics as these involve an analysis of sales so as to obtain the figures for each assistant, but this will be necessary in any case where commission is paid.

**Customers.** Many concerns, particularly departmental stores and multiple shops, will collect statistics of the number of customers served, dividing them under the headings of cash and credit transactions. In order to do this a separate counter slip must be made out in respect of every sale, and these may be summarised daily and entered on a report in the form shown. The number of sales made, if analysed departmentally, again acts as an index of the number of assistants needed.

### SHOP REPORT

for Monday, 12th November, 19..

Department	Cash Sales				Credit Sales			
	Number	Amount			Number	Amount		
A	75	25	10	6	15	9	7	6
B	92	32	4	5	54	29	18	4
C	84	34	2	7	75	33	4	2
D	10	30	5	6	20	45	2	0
Total for Day	261	122	3	0	164	117	12	0
Total for Month to Date	2936	1542	19	8	1842	1370	4	9



**Profits.** The net profit of the business will be ascertained from the retailer's profit and loss account, due regard being paid to such matters as the remuneration of the proprietor, and an allowance for rent when he occupies his own premises. The net profit may be expressed as a percentage of the turnover for purposes of comparison.

**MODERN TENDENCIES IN THE RETAIL TRADE.**—The structure of retail trading has undergone considerable modification in the post-war period, though, as already indicated, the standard of efficiency is still deplorably low. It has been estimated that in England and Wales, there is on an average about one retail shop to every sixty persons, with the result that the average small shopkeeper cannot hope to create a sufficient turnover to yield him a satisfactory income without charging his customers directly or indirectly more than his services are worth. Yet the need for efficiency in retailing is greater to-day than ever in the past. About three-fifths of the articles sold through retail shops in the United Kingdom fall in the category of food and perishables. In connection with many of these—for example, milk, eggs, bacon, and meat—primary producers are forming *marketing boards* with wide statutory powers, and the impact of these organisations on the retail distributor will soon make itself felt. If the distributor is to hold his own he will have to organise as well.

It is, of course, true that there has been a tendency for large-scale organisations, such as departmental stores and multiple shops, to increase their share of the total trade at the expense of the small trader. These organisations are introducing scientific methods in the sphere of retail distribution with a consequent increase of efficiency. There is, none the less, ample scope in the retail trade for the small trader who knows his business. Again, the advance of the consumers' co-operative movement has caused considerable concern of recent years to private trading interests. Yet, as one Government Committee<sup>1</sup> has pointed out, the inroads which have been made by this system of trading are certainly no greater than those made by large-scale retailing concerns, such as multiple shops and departmental stores.

In addition to the foregoing considerations, however, the character of the retail trade has been affected by the following developments—

<sup>1</sup> Report of the Committee Appointed to Inquire into the Present Position of Co-operative Societies in Relation to Income Tax. Cmd. 4260.



(1) **Branding Goods.** A growing number of goods which at one time were sold in bulk are now sold ready packed under a special name. The practice of branding was introduced by manufacturers who desired to develop national distribution of a commodity with the aid of national advertising. In this way the individuality of a product may be established with the result that a higher degree of control over prices, demand, and trade channels may be established than would otherwise be possible. Where a manufacturer deals in branded goods, his advertising can be linked definitely with his own product so that consumer demand is created, not for, say, tobacco in general, but for a stipulated brand of tobacco. In this way retailers and wholesalers are compelled to hold stocks in order to meet the consumer demand, whilst at the same time the retailer loses some of his power to influence the demand of customers. Such goods usually carry a smaller margin of profit to the retailer than is the case with unbranded goods, the argument being that they are more easily handled by the retailer.

Competition between manufacturers has, however, brought into existence in the case of most commodities rival brands of merchandise, which, from the standpoint of the consumer, differ little one from the other. The proprietors of the rival brands attempt to establish them by expensive advertising campaigns, with the result that the cost of advertising has shown considerable increase since the War. At the same time the difficulties of the retailer are increased since he has to stock a number of lines in order to cater for the varying demands of his customers. The general confusion has been further intensified by the fact that many wholesalers and large retailers have introduced private brands which they sell in competition with those of the manufacturers. Such goods can generally be bought more cheaply than branded goods which are nationally advertised, so that larger margins of profit can be realised. Secondly, in the case of a wholesaler, such brands give a greater sense of security. He may work up a business for a manufacturer and then have it taken away by a decision of the latter to sell direct to retailers. If the wholesaler has his own private brand this cannot occur.

(2) **Price Maintenance.** Closely allied with the development of the sale of branded goods in the retail trade is the vexed question of resale price maintenance. Branded goods which are widely advertised



are almost invariably price maintained, the retail selling price figuring in the advertisements. Amongst the trades in which the system is most prevalent are books, newspapers and periodicals, stationery, drugs, photographic goods, gramophones and records, motors and cycles, tobacco and cigarettes, confectionery and groceries. It is less widespread in the drapery and clothing trades. Some trades, especially those which handle fashion goods or highly perishable goods, are scarcely affected.<sup>1</sup> A retailer may use well-known proprietary articles as "leading lines," hoping that, by selling them below the standard price, he will attract custom to his shop for other goods. Such a practice immediately antagonises the neighbouring retailers who find their sales falling off. This may lead them either to cut prices in competition or to discontinue stocking the line in question, so that the manufacturer's sales fall off.

In order to enforce the observance of the retail prices fixed by him, the manufacturer usually employs persuasion in the first place, then the threat of withholding supplies, and finally the actual withholding of supplies. The last course of action is one which is not always easily taken since often the channels of distribution are so complicated that the source of supplies cannot be located. In consequence, in certain trades manufacturers have combined in associations for the purpose of detecting and suppressing price cutting. Such associations are in existence in the drug, publishing, stationery, motor, grocery, and tobacco trades. In so far as this policy of price maintenance can be enforced, competition in such articles in the retail trade ceases to be on a basis of price, so that the profit margin of each retailer will depend on his efficiency in reducing costs.

**(3) Gift Coupons.** This is a form of propaganda adopted by the manufacturers of proprietary articles, under which coupons are issued redeemable in goods which are for the most part not produced by the issuer of the coupons. In some trades, such as the soap and tea trades, it has long been the practice of certain producers to issue with their goods coupons which may be presented in specified numerical quantities for redemption in "gift" articles. The growth of competition in recent years has caused an appreciable extension of the scheme and it has been adopted by many new trades. Such a

<sup>1</sup> Report of Committee appointed by the Lord Chancellor and the President of the Board of Trade to consider Certain Trade Practices.



scheme is applicable only to branded goods in constant demand, so that the number of coupons requisite to obtain a gift can be collected within a reasonable time. By far the greater number of gift coupon schemes are in connection with the sale of food, soap, and cigarettes.

The question of coupon trading has excited a great deal of controversy in recent years, and the following arguments have been brought against the practice<sup>1</sup>—

(a) That the purchaser of the coupon-bearing article is led to disregard its quality or value and to concentrate his attention upon the accompanying gift, being misled into the belief that he is getting something for nothing.

(b) That the distribution of gifts by manufacturers of consumable goods involves the setting up of a secondary system of distribution destroying the trade of the retailer of the goods given away, while adding to his uncertainties by reason of the spasmodic character of many gift distributions, and that the public will suffer by losing his specialised services, or will have to provide a larger margin of profit on the other goods which he sells.

(c) That manufacturers are tempted to put down extra plant for the production of coupon "gifts" which may prove to be a purely ephemeral demand.

(d) That, while gift coupons may stimulate the sales of those firms in an industry which first adopt them, this is likely to be largely at the expense of other firms, which are compelled in self-defence to follow suit: the result being that the forces of competition come into play in regard to the gift schemes themselves, and a wasteful expenditure of money and effort is incurred by the industry in distributing products in which it has no real interest.

On the other hand, those firms using the scheme as a method of sales promotion have put forward the following arguments—

(a) That they enable the public to secure in the form of a gift part at any rate of the money which must in any case be spent by the manufacturer in promoting sales; and in so far as they do this they represent a benefit to the public, whose purchasing power is undiminished.

(b) That the cost incurred by the manufacturer in distributing gift good is materially less than the cost of distribution through

<sup>1</sup> The Report of the Committee on Gift Coupons and Trading Stamps Cmd. 4385.



ordinary wholesale and retail channels, and that the difference accrues to the advantage of the public.

(c) That gift coupons facilitate saving by the public.

(d) That gift coupons represent a means by which a new or small firm can gain a footing in the trade against well-established concerns, because expenditure on gift coupons is virtually in direct proportion to sales.

### TEST PAPER XXV

1. Show, by taking the grocer as an example, what are the functions of the retail trader.

2. Give examples of different types of retailers to be found in modern business and explain the nature of the services they render to the home manufacturer.

3. It has been stated that the only function remaining now for the small trader is to open up in a new district with a growing population and to develop business which he is destined to lose in a short time to multiple shop firms and central department stores. Discuss this view, and set out what you yourself consider the proper sphere of the small shopkeeper in modern trade.

4. What are the types of organisation engaged in the retail trade? Give a detailed account of any one of them and state how it is specially organised to satisfy public demand.

5. A retail trader usually carries stock which costs him £2,500. He turns over his stock four and a half times a year and he makes 20 per cent gross profit on sales. His total expenses usually amount to £1,500. Find his annual gross profit and his annual net profit; and express each as a percentage of his turnover.

6. A retailer has premises valued at £4,500 and stock which cost him £2,500. He owes £600. He turns over his stock four times each year, making 20 per cent gross profit on his sales each time. His expenses amount to £500 for the year. What percentage does his net profit bear to his capital?

7. The ratio of total expenses to sales taken over a period of a year is sometimes referred to as the "Operating Ratio." Consider how far its fluctuations year by year can be taken as indices of the progress of a retail business.

8. Outline the chief outstanding statistical facts which, in your opinion, are vitally important to a large retail business and by which its yearly progress can best be examined and adjudged.

9. Draw up in outline, a statement of gross sales for a shop in any branch of retail trade selected by yourself, and explain what further information is needed in order to ascertain net sales.

10. Discuss the advantages and disadvantages of "branded" goods in retail trade. Why do traders often sell goods under their own private brands when it is evident they are not manufacturers?

11. It has been stated that "the policy of price maintenance imposed by manufacturers on retailers is of little importance." Do you agree? Argue the points involved.

12. Discuss the effect upon the retail trade of the increase in proprietary articles sold at prices fixed by the manufacturers.

13. Discuss the reasons for the increase in the average size of the retail business unit, and indicate the advantages and disadvantages of this trend.



## CHAPTER XXVI

### TRANSACTIONS IN THE RETAIL TRADE

**BUYING IN THE RETAIL TRADE.**—The retail dealer assembles a stock of goods from which his clients may select their requirements, whilst the retailer himself obtains his stock either from the original producer or from some form of wholesaler. In a later chapter we shall examine the various channels through which goods may pass from producer to consumer, but for the moment we may regard these two as the principal sources of supply, whilst in the case of the small retail trader the wholesaler is the most important. A retailer of the type we are considering, upon establishing himself in business, will wish to get into contact with one or more wholesalers who can supply his requirements. This he may do by making a written application for their price lists and terms of sale, but before he has been in business long he will be waited upon by travellers of manufacturers and wholesalers who are active in the district. These will supply him with price lists and show him samples of the goods which they supply and will also take any orders which he has to give. The price list will probably display the items on lines similar to the specimen reproduced on page 298. In most cases where branded articles are being sold the supplier will state in the list not only the wholesale price to the retailer, but also the minimum selling price which must be charged to the consumer. This system of "price maintenance," as it is termed, is employed to prevent one dealer undercutting another in the sale of proprietary articles. In these price lists will also be found the conditions of sale of the wholesale house covering such matters as discounts, time of payment, mode of delivery, and similar matters.

In some trades, however, it may not be possible to draw up a standard price list on these lines, or if such a list can be supplied, the requirements of the trader may necessitate special treatment. Thus, he may be buying exceptionally large quantities, or he may require some special mode of packing. In these circumstances, the trader will address a special inquiry to the wholesale house asking for a special *Quotation*. This may be described as a particularised



# SPECIMEN PRICE LIST

## WHOLESALE GROCERY SUPPLIES, LTD.

### CURRENT PRICE LIST

#### "EXCELSIOR" SHREDDED BEEF SUET

Size	PRICE TO	
	Retailer	Consumer
Loose in 28's . . .	11½d. per lb.	—
Loose in 7's . . .	1/- "	—
1 lb. Cartons . . .	1/0½ "	1/3½ per lb.
½ lb. Cartons . . .	1/0¾ "	1/4 "
¼ lb. Cartons . . .	1/2¼ "	1/6 "
* Small Packets . . .	19/- per gross	2d. each

#### "EXCELSIOR" BLOCK SUET (in Cartons)

	PRICE TO	
	Retailer	Consumer
1 lb. Cartons . . .	1/0½ per lb.	1/3½ per lb.
½ lb. Cartons . . .	1/0¾ "	1/4 "
¼ lb. Cartons . . .	1/2¼ "	1/6 "
* Small Blocks . . .	14/- per gross	1½d. each

#### "EXCELSIOR" BLOCK (in Decorated Airtight Tins)

	PRICE TO	
	Retailer	Consumer
1 lb. Tins . . . . .	1/1	1/4

CARRIAGE PAID, NET CASH, 30 DAYS.

\* The Small Packets and Small Blocks are packed 3 doz. to the box in neat, decorated boxes for counter display.

*Please state clearly whether Shredded or Block is required.*



form of price list and comprises a statement of the price and terms upon which certain articles can be supplied. In somewhat the same category is the *tender* or estimate which may have to be submitted by the retailer himself. This method of obtaining prices for supplies of goods is usually adopted by large commercial buyers and public authorities. They will usually insert advertisements in the Press inviting tenders for certain classes of goods, the tenders having to be made on official forms. These tender forms usually state in detail the conditions of contract and specify the nature of the goods to be supplied. They are filled in by the retailer and returned, though there is no binding contract until the tender has been accepted. A specimen is shown on pages 300 and 301.

Reverting now to the procedure of the retailer who is considering the purchase of goods for stock we may assume that he is in possession of prices upon which he can base his *Order*. Before placing the order with the supplier he will have to decide what quantities of goods he is to order, and his decision will be influenced by—

- (1) The warehousing accommodation which is available.
- (2) The speed with which the goods can be sold—a matter which must be settled either by his past experience or by his estimate of the possibilities of the market.
- (3) The durability of the product in view of the storage conditions which he can provide.
- (4) The length of time which it will take to obtain new supplies.
- (5) The terms which the supplier offers for orders of varying size.

In purchasing supplies the last factor is frequently allowed to exert an undue influence on the mind of the retailer who may be tempted into a policy of over-buying on account of the possibility of securing quantity discounts or “bargain” prices. This is a fatal mistake, for if goods are purchased in quantities which are too large, not only is an excessive amount of capital locked up in them, but the trader is exposed to the risk of loss due to physical deterioration or on account of changes of fashion. On the other hand, if goods are bought in quantities which are too small, there is a danger of running out of stock, which results in loss of custom and injury to goodwill. A further question which may have to be settled in the case of packaged goods is the size or sizes of package which shall be ordered. The makers may pack the goods in half a dozen different sizes, but it does not follow that all of these will be in equal demand



## SPECIMEN TENDER FORM

### SOUTH WALES COLLIERIES, LTD.

#### CONDITIONS OF CONTRACT FOR NAILS, ETC.

This Contract shall extend over a period of six months, from 1st Jan., 19 . . to 30th June, 19 . . , and the Contractor shall supply any of the Articles specified in the accompanying Schedule at the prices affixed thereto, and in such quantities as shall from time to time be ordered. They shall be supplied within a reasonable time after the order is given, and *delivered* by the Contractor at his own *risk* and *expense* at the Colliery stated on the order.

The Articles shall be supplied to, and be equal in all respects to the Samples, Patterns, or Specifications of the Company, and where no Samples or Patterns are exhibited, or Specifications mentioned, then the Articles shall be the best of their respective kinds, and the decision of the Company thereon shall be binding and conclusive in all cases.

If the Contractor objects to supply any Articles mentioned in this Schedule to which he has affixed a price (upon notification of the Company's acceptance of it), or shall fail to supply such Article within ten days after the Order shall have been given, the Company shall have power to purchase from any other party, and charge the Contractor with the difference (if any) between the cost of such Article and the contract price, and deduct the same from the moneys which may be or in any time afterwards become due to the Contractor, or be recoverable as a debt, and, further, should the Contractor commit a breach of contract the Company shall, either before or after the exercise of the powers above mentioned, be at liberty to terminate the Contract by a notice in writing to that effect.

The Contractor shall, if required, give such security for the due performance of the contract as the Company may approve.

The Contractor is to provide, at his own expense, all kegs, packages, etc. No charge will be allowed for packages under any circumstances, whether returned or not.

The net weight, measurement, or number ascertained by the Company at the time of delivery to be conclusive for all purposes.

The Contractor is not to sub-let or transfer the Contract ~~to~~ any person whatever without the consent of the Company having been first obtained in writing.

Payment at the end of the month after delivery, LESS 2½ PER CENT DISCOUNT.

A priced Invoice, bearing the Order number, must be transmitted to the Company at Treorchy, Rhondda, immediately after the dispatch of each lot of goods.

No goods to be supplied without an Official Order from the Company.

The Company do not bind themselves to accept the lowest or any Tender, and they shall be entitled to accept any part of a Tender.

*Contractors to the Company who may offer or pay Commission or give Gratuities to the Company's Staff thereby forfeit their right to supply the Company with goods, and no Tenders from such persons will be considered.*



## TENDER

WE, *T. Yates and Sons*, hereby Tender and, provided this Tender be accepted, hereby contract and agree to supply **SOUTH WALES COLLIERIES, LTD.**, from 1st *January*, 19 . . to 30th *June*, 19 . . on the terms and conditions set forth in the above Specification, with any of the Articles enumerated in the following Schedule, to which we have affixed a price, and agree to abide by and fulfil all the forms and stipulations specified.

Dated this *tenth* day of *December*, 19 . .

Signed *T. Yates and Sons*.

Address *45 Queen Street,*  
*Cardiff.*

### NAILS, ETC.

No.	Description	Price																		
1	<b>Horse Nails, "E," "Mustad" Brands, viz.—</b>  Size No. . . . . Lots 40 boxes, price per 25 lb. box ,, 20 ,, do. .	<table><tr><td>4</td><td>5</td><td>6</td><td>7</td><td>8</td><td>9</td><td>10</td><td>11</td><td>12</td></tr><tr><td>4/-</td><td>4/6</td><td>4/6</td><td>5/-</td><td>5/-</td><td>5/6</td><td>6/-</td><td>6/6</td><td>7/-</td></tr></table>	4	5	6	7	8	9	10	11	12	4/-	4/6	4/6	5/-	5/-	5/6	6/-	6/6	7/-
4	5	6	7	8	9	10	11	12												
4/-	4/6	4/6	5/-	5/-	5/6	6/-	6/6	7/-												
2	<b>Wrot-Iron Brattice Nails, size <math>\frac{3}{4}</math> in. . . . .</b>	per cwt.																		
3	<b>Strong Rose Flat Points, viz.—</b>  Size . . . . . 2 ton lots, price per cwt. 1 ,, ,, ,, ,, Under 1 ,, ,, ,, ,,	<table><tr><td>1½</td><td>2</td><td>2½</td><td>3</td><td>3¾</td><td>4</td><td>5</td><td>6</td></tr><tr><td>16/-</td><td>16/3</td><td>17/-</td><td>17/3</td><td>18/-</td><td>18/3</td><td>19/-</td><td>19/3</td></tr></table>	1½	2	2½	3	3¾	4	5	6	16/-	16/3	17/-	17/3	18/-	18/3	19/-	19/3		
1½	2	2½	3	3¾	4	5	6													
16/-	16/3	17/-	17/3	18/-	18/3	19/-	19/3													
4	<b>Steel Cut Nails, viz.—</b>  Size . . . . . 2 ton lots, price per cwt. 1 ,, ,, ,, ,, Under 1 ,, ,, ,, ,,	<table><tr><td>1½</td><td>2</td><td>2½</td><td>3</td><td>3¾</td><td>4</td><td>5</td><td>6</td></tr><tr><td>15/-</td><td>15/6</td><td>16/-</td><td>17/-</td><td>18/-</td><td>19/-</td><td>21/-</td><td>25/-</td></tr></table>	1½	2	2½	3	3¾	4	5	6	15/-	15/6	16/-	17/-	18/-	19/-	21/-	25/-		
1½	2	2½	3	3¾	4	5	6													
15/-	15/6	16/-	17/-	18/-	19/-	21/-	25/-													



## SPECIMEN ORDER FORM

### ORDER

No. A 397

Telephone: Cardiff 432

#### A. SMALLMAN AND SON

Retail Grocers and Provision Dealers

21 City Road,  
Cardiff.

24th October, 19

*The Wholesale Grocery Supplies, Ltd.,  
17 Eastcheap, London, E.C.3.*

Please supply the following goods—

1 gross small packets "Excelsior" Shredded Beef Suet @  
19/- per gross.

2 doz. 1 lb. Jars "Radion" Brand Apricot Jam @  
6/6 per doz.

2 doz. 2 lb. Jars "Radion" Brand Greengage Jam @  
12/6 per doz.

Terms: *Net cash, 30 days.*

Delivery: *Earliest, to above address.*

For and on behalf of

A. SMALLMAN & SON.

*T. Smallman,*

*(Manager)*

Please note—

No order will be recognised unless given on our official order forms and duly signed.

We reserve the right to reject any goods which are not in accordance with the description given above.

An advice note should be sent with every consignment.

The number of this order should be quoted on all invoices.



amongst the retailers' customers. Here again is a matter in which experience is the only reliable guide.

When the trader has settled these preliminaries in his own mind, he can then proceed to order the goods. All orders should be given in writing and a copy retained, the usual practice being for the small trader to use a *Duplicate Order Book*, in which a copy of every order is made by means of a carbon paper, the original being torn out and sent to the supplier. Each order and copy are numbered serially so that by quoting the order number and date, adequate reference may be made to any order. The order will be made out on the lines indicated in the specimen given on page 302. Care must be taken that in all cases full details of the quantities, price and description of the goods are given together with any special instructions as to packing and delivery. Particular care should always be taken in regard to these matters, otherwise mistakes are always liable to arise which may occasion inconvenience and delay.

Upon receipt of the order, the wholesale house will send a formal acknowledgment, thanking the retailer for the order and probably giving some indication of when delivery may be expected. In the case of an opening order the wholesale firm will require to know something of the standing of the retailer before opening a credit account with him. The retailer may have given trade references in which case these will be investigated before the goods are sent. If no references have been given, a status inquiry may be sent to a *Trade Protection Association* or a tactful letter may be addressed to the trader pointing out that, as this is a first transaction, it is customary to ask for trade references. When these preliminaries are settled, the goods are prepared and dispatched. They may be sent either in the wholesaler's own vehicle or by an independent carrier. In either case, when the goods are delivered, the retailer will be required to sign some form of delivery book or *Delivery Note*, stating that the goods have been received. As there is usually not time to make a proper examination of the consignment immediately on arrival, many persons mark the sheet "not examined" with the idea of leaving the way open for making a claim should this prove necessary. In any case, the recipient of the goods does not lose his right to reject damaged or unsuitable goods until he has had a reasonable opportunity of examining them. Many firms draw the attention of their customers to the need for prompt notification of



# SPECIMEN INVOICE

## INVOICE

26th October, 19. .

Bought of

**THE WHOLESALE GROCERY SUPPLIES, LIMITED**

17 EASTCHEAP,

LONDON, E.C.3.

*Messrs. A. Smallman and Son,  
21 City Road,  
Cardiff.*

Order No. A397

Per G.W.R. Goods

Carriage Paid

			£	s.	d.
1	gross Small Packets "Excelsior"				
	Shredded Beef Suet per gross	19/-		19	0
2	doz. 1 lb. Jars "Radion" Brand				
	Apricot Jam per doz.	6/6		13	0
2	doz. 2 lb. Jars "Radion" Brand				
	Greengage Jam per doz.	12/6	1	5	0
			2	17	0

E. & O. E.

Net Cash, 30 days.



damage to consignments by printing on their *Advice Notes* or *Invoices* some such clause as the following—

No claim on account of short delivery, damage in transit, or other causes will be admitted unless made within four days of delivery of these goods.

On the same day as the goods are dispatched by the wholesaler he will send an *Advice Note* to the retailer informing him that the goods, which are specified in detail, have been dispatched to him and indicating the mode of transport employed. Alternatively the *Advice Note* may be dispensed with, and an invoice on the lines of the example on page 304 sent instead. The invoice should show details of the quantities, descriptions, and prices of the goods, together with any trade discounts which may be allowed. Reference should be made to the number of the customer's order and also to any special terms of payment, cash discounts, etc. The distinction between trade and cash discount has already been referred to on page 258. Finally, if the invoice is being used as an *Advice Note*, a reference to the mode of delivery will be necessary. Upon receipt of this document, the goods will be checked by it and also with the original order so that any material discrepancies can be brought to the notice of the supplier and a claim entered accordingly. If any charge has been made on the invoice to cover cost of carriage, reference should be made to the wholesaler's conditions of sale to see whether this is in order. Generally speaking, most wholesale houses pay carriage on all orders over a certain value, and an attempt should be made whenever possible to give an order sufficiently big to avoid payment of carriage.

Any adjustment which may be necessary between buyer and seller on account of some mistake in the original invoice, or of a claim made for damage or unsatisfactory goods, may be made in one of two ways. The supplier, having agreed to the claim may submit an amended invoice which supersedes the first. More usually, however, he will make the correction by sending a *Credit Note*. Thus, we will assume that the wholesaler undertakes to pay carriage on all orders valued £5 and over, but has by oversight charged carriage on an order for goods exceeding this value. He will then send out a credit note in the form shown in the example on page 306, this document usually being printed in red ink so that it may readily be distinguished from an invoice.

At the end of each month, or sometimes at the end of each



## SPECIMEN CREDIT NOTE

## CREDIT NOTE

30th October, 19. .

Credit by

**THE WHOLESALE GROCERY SUPPLIES, LIMITED**

17 EASTCHEAP,

LONDON, E.C.3.

*Messrs. A. Smallman and Son,  
21 City Road,  
Cardiff.*

			£	s.	d.
	By allowance in respect of $\frac{1}{2}$ doz. 2 lb.				
	Jars "Radion" Brand Greengage				
	Jam, broken in transit, invoiced on				
	26th October, 19. .			6	3

quarter, the supplier will send out a *Statement of Account* which shows in summary form the state of indebtedness between the two firms. The dates and amounts of each consignment will be given but no details appear since these have already been shown on the individual invoices. Likewise all allowances which have been made will be indicated. The document will appear in the form shown on page 307. Upon receiving it, the retailer will check it with the entries made in his own books of account and, having satisfied himself that it is in order, will send a remittance accordingly. By the use of the Statement the two parties are enabled to discover and rectify any discrepancies in their books periodically so that items are not



# SPECIMEN STATEMENT AND RECEIPT

## STATEMENT

31st October, 19. .

*In account with*

**THE WHOLESALE GROCERY SUPPLIES, LIMITED**

17 EASTCHEAP,

LONDON, E.C.3.

*Messrs. A. Smallman and Son,*

21 City Road,

\* *Cardiff.*

			£	s.	d.	£	s.	d.
Oct.	26	To Goods . . . . .	2	17	-			
„	30	Less Allowance as per Credit Note . . . . .		6	3	2	10	9

No. B 38765

6th November, 19. .

*Received for*  
**The Wholesale Grocery Supplies, Limited**  
 17, Eastcheap, London, E.C.3

From  
*Messrs. A Smallman & Son*  
 the sum of *two pounds*  
*ten shillings and nine pence*

£2 : 10 : 9

2d.  
Stamp  
*J. R. Jones*

Terms: Net cash, 30 days.

Receipts are valid only when upon our Official Form.

Cheques, etc., should be made payable to The Wholesale Grocery Supplies Limited.



overlooked for long periods of time. In making payment, a covering letter will usually be sent with the remittance stating which items it is intended to cover. Alternatively, some type of *Cheque Enclosure Form* may be employed giving substantially the same information, though this latter document is more likely to be used by a large firm having numerous payments to make than a small one. In due course a *Receipt* will be received from the supplier in acknowledgment.

**COLLECTION OF ACCOUNTS.**—It should be the aim of every business to develop in customers the habit of making payments promptly. There are four main reasons for this—

(1) Experience shows that the bulk of the losses incurred from accounts receivable are from those overdue. It is almost invariably the person whose accounts are allowed to run unpaid who fails.

(2) By keeping accounts paid in promptly less capital is required. For instance, £6,000 might be adequate to run a business where otherwise £7,000 would probably be required without any increase in the net profits.

(3) Especially with retail houses, prompt collections increase sales because many customers, if an account has run a length of time, dislike to continue buying from that house until it is paid. Besides as the retail dealer has no such hold on his customer as the wholesaler, his risk is generally greater by letting an account run than is the case with the wholesale house.

(4) Dispute is less likely to occur over an account if attended to promptly; thus there is less probability of the necessity for stringent means to be employed, which is always undesirable from a business standpoint.

**METHOD OF HANDLING COLLECTIONS.**—The following is a method of handling the collection of accounts. In the first place a statement of all due accounts should be made out in duplicate; the original statement is sent to the debtor; the duplicate carbon copy is placed in a follow-up folder file. If it is thought that a certain account should be paid in ten days, the duplicate copy is filed forward this length of time; that is to say, if the account is sent out on the 3rd of the month the duplicate copy is filed in the folder behind the guide for the 13th, on which date the account will automatically present itself.

On the 13th reference is made to see if a reply has been received;



if not, a letter may be sent, a copy of which, together with the duplicate account, is filed ahead another ten days or any other desired length of time. If the copies of the letters are kept in bound form, then a note on the duplicate of the account may be made indicating where the copy will be found; on the account will also be indicated the ledger folio, so that reference to the ledger account can easily be made.

A series of form letters is of value in the collection department, but must not be wholly relied on. Generally speaking, however, consecutive form letters may be prepared and sent to delinquent debtors, thus avoiding the necessity of personally dictating every letter. The pressure brought to bear in these letters should be graded, increasing as the number of letters sent unheeded increases.

In some cases Statements are addressed to the debtor, containing remarks which increase in severity with the number of applications for payment; e.g.—

2nd Application—A/c overdue.

3rd Application—A/c much overdue.

4th and Final Application.

**Monthly Instalment Accounts.** Instalment accounts are constantly changing and any system planned for handling such accounts should provide for the elimination of all dead matter. This may be done by keeping the accounts on cards; one side of the card may be used for a digest of the original contract, the other side for the account and record of the payments, with a column for the balance.

Paid-up accounts should be kept in one index, delinquents should be kept in another.

At the beginning of the month, or at a certain specified time, all due accounts will be in one file. As payments are made they are entered on the respective cards, which are then placed in the file for paid-up accounts, thus eliminating them from the unpaid accounts. By the end of the month all the payments should have been made, and the cards will then have been transferred to the second file, which will contain the unpaid accounts for the next month. All accounts that are not paid up should be removed and followed up closely until paid.



## TEST PAPER XXVI.

## GOODMAN &amp; SONS, LTD.

*Importers and Wholesale Provision Merchants*

BUTE STREET, CARDIFF

Terms: 2½ per cent for payment within ten days.

## PRICE LIST (continued)

All prices are subject to alteration at any moment.

<i>Bacon</i>			<i>Hams</i>		
Irish Sides . . .	125/-		Short Cut . . .	98/6	
Danish . . .	117/-		Longs . . .	96/6	
Canadian Wilts . . .	97/6		Squares . . .	71/-	
Cumberlands . . .	95/6		Picnics . . .	68/6	

1. The above is part of a page from Messrs. Goodman & Sons' Price List. Assume that you are a retail grocer and order a selection of goods from this part of the price list. Draft the whole of the correspondence and the documents that will pass between you and Messrs. Goodman up to the completion of the transaction.

2. Develop a suitable "Tender Form" for the sale of hardware goods, indicating the descriptive and protective clauses necessary to cover the seller's liability.

3. A retailer has before him a number of quotations for the same class of goods from wholesale warehouse men. Point out the various factors he must consider before deciding which to accept.

4. What particulars should be given in an invoice? Compare this document with a statement of account, and give an example of the latter containing at least four items.

5. Explain the purpose of "cash discount" and "trade discount," and the circumstances under which each is given.

A buys from a wholesale merchant goods to the value of £50 less 25 per cent on the following terms as to payment: for cash on receipt of invoice, 5 per cent; monthly account, 2½ per cent; three months' account, net. What amount is due—

- if cash is paid on receipt of invoice;
- if payment is made at the end of a month;
- if he postpones payment until the end of three months?

6. What is a credit note and for what purposes is it used?

7. Make out an invoice in proper form for the following goods sold by Robert Jones & Sons, Ltd., Wholesale Grocers, Kirkgate, Wakefield, to William Smith, Main Street, Doncaster, on 2nd March last—

6 doz. packets Porridge oats @ 6s. 9d. per doz.

3 doz. tins pineapple @ 7s. 3d. per doz.

4 doz. O.K. sauce @ 72s. per gross.

6 doz. A.G. tongues @ 9s. 9d. per doz.

Terms: Trade discount 10 per cent, and 2½ per cent for cash within 10 days.

8. William Smith paid the account referred to in Question 7 on 10th March. Enumerate the various means of remittance which he could employ, and give a copy of the receipt which would be sent to him in acknowledgment.

9. What system would you adopt for the collection of overdue accounts?



## CHAPTER XXVII

### THE DEPARTMENTAL STORE

THE departmental store represents one of the forms which large-scale retailing has assumed in recent years. It is possible for expansion of the retail unit to occur in one of two ways: either the size of the individual store may be enlarged in order to undertake a greater volume of business, or the concern may establish branches in other localities in order to open up new retail markets. This second alternative gives rise to the multiple shop systems which are discussed in the following chapter and we shall here concern ourselves with the first type. Now it is a well-known principle of economics that the expansion of an enterprise is limited by the *extent of the market*, and this principle applies in the sphere of distribution as well as in production. If a retail business grows by the expansion of its premises in one location, there is a limit to its turnover of any given class of goods, and this limit will depend upon the number of retail customers which it can attract. Advertising coupled with modern transport developments has enlarged considerably the sphere of influence of such a retail organisation, but if it adheres to its original line of business in the majority of cases its turnover will be definitely limited. In order to escape from this dilemma the proprietors may elect to diversify the business and to stock other classes of goods so that the same customers may be induced to spend a larger proportion of their incomes within the establishment. Thus the departmental store comes into existence.

In England, departmental stores and bazaars first came into existence between the "forties" and "sixties" of the nineteenth century, and some of the early undertakings, such as Whiteley's and Peter Robinson's, are still flourishing. The greatest development of these stores has been in France, however, where the idea was first conceived, the chief examples being the "Bon Marché!" and the "Louvre" in Paris. The majority of departmental stores appear to have come into existence as the result of expansion; there are very few examples of a store being started as the result of



a definitely conceived plan. In a very large number of cases, too, the departmental store has its origins in a drapery establishment. This type of business appears to lend itself to the introduction of allied departments in order to attract further custom. In this connection, too, it may be noted that even to-day the departmental store makes its greatest appeal to women.

**CAUSES OF DEVELOPMENT.**—As we have already indicated, one of the essentials for the development of the departmental store is the presence of a large retail market, so that the growth in the size of the towns in the latter half of the nineteenth century contributed to their development. In order that the shop may gain the full benefit of such a market, it must be situated so as to be readily accessible—in other words, it must be located in a recognized shopping centre. The development of transport facilitated by road and rail in the last few years have tended to strengthen its position in this respect, by widening its market and making it easier for customers to do their shopping. In the same connection, too, the development of the motor vehicle has improved the service of the store to its customers by making speedy delivery an easy matter. Again, although the chief success of the departmental store has been achieved in respect of “shopping” lines, i.e. goods which the consumer purchases only occasionally and wishes to make comparisons before choosing; in recent years considerable extensions have been made in “convenience” lines as well, i.e. goods which are continually required for domestic purposes. The fact that such goods can be ordered by telephone and delivered almost immediately by van has assisted the departmental store immensely in this line of business. From this it must not be inferred, however, that the departmental store is likely to supersede the small shop-keeper. The incomes and buying habits of a large section of the population would prevent such an occurrence.

Finally, the extension of press advertising has further consolidated the position of the departmental store by enabling it to reach and influence the minds of a great number of potential customers. The resources of the store are considerably greater than those of the average independent shop, and in consequence it is in a strong position to undertake this expenditure. Moreover, most of the large departmental stores have developed a mail-order department in order to attract the custom of those whom distance prevents from



shopping in person. Many of the stores have an extensive mailing list of customers whom they circularise periodically with price lists and catalogues. All this publicity strengthens the hold of the store on the retail market and assists in its expansion.

**ORGANISATION OF THE DEPARTMENTAL STORE.**—The precise details of the organisation of a departmental store vary with the size and the type of business concerned, but the following details afford an indication of the system usually employed. From the standpoint of its legal constitution, the departmental store is usually a limited company so that the ultimate control of policy is vested in the Board of Directors. The actual operations of the business, however, are supervised by a Managing Director, who will be concerned with the general co-ordination of all the activities carried on. The detailed control of the specialised activities of the business will be delegated by him to a series of sectional managers, the customary divisions being Merchandising (including Purchasing and Selling), Staff Management, Maintenance and Service, Advertising, and Accounting and Finance.

(1) **Merchandising.** This section which is the actual profit-earning department of the business is under the control of the Merchandise Manager, and comprises the associated activities of buying and selling. The section is divided into a large number of selling departments—between one and two hundred in some cases—and at the head of each is a buyer. In some cases where the departments are small, one buyer may control a group of associated departments. Although the general buying and selling policies of the store will be controlled by the Merchandise Manager, the success or failure of a particular department depends largely upon the buyer. In planning the buying for the store it is necessary to make a detailed study of the area served and the nature of the competition to which the concern is exposed. In drawing up a buying programme the buyer can be assisted greatly by statistical records of departmental turnover in former seasons, but in addition a buyer must exercise a kind of instinctive judgment, based on experience and close study of his market as to which lines are most likely to find favour. In this respect he may be assisted by a system of "Want Slips" or "Lost Order Slips" which record inquiries for merchandise which was not in stock.

The difficulties of departmental store merchandising are intensified



by reason of the large part which style plays in the selection of goods. On account of the wide variety of colours and styles, and because of the rapid changes, seasonal and otherwise, it becomes necessary to keep stock down to a minimum. At the same time it is necessary to buy on such a scale as will enable all customers' orders to be executed, for an under-estimate of requirements often cannot be rectified by re-ordering. Manufacturers or wholesalers may have no stocks left on hand. At the same time the buyer must not "over-buy" any particular line since this will entail his having unsold stocks left on his hands which can be sold only after a heavy "mark down," which eats into the profits of his department. Departmental store merchandising is, therefore, a highly skilled business, requiring close contact with the selling side—a fact which explains why the head of each selling department discharges the function of buyer.

(2) **Staff Management.** The size of the staff engaged in a large departmental store warrants the creation of a special department under a Staff Manager to deal with the problems of personnel. A number of substantial advantages are to be gained by the introduction of such a department. In the first place the work of staff supervision and selection is concentrated in one office so that a uniform policy may be put into operation in respect of it. Departmental managers are sufficiently occupied in the supervision of their own departments and can have no time to spare for the routine work of staff recruiting. Again, such a department can make effective use of the available labour force by providing for the transfer of staffs from one section to another in exceptionally busy times, whilst the employment of temporary assistants can be placed on a proper basis. Such a department also acts as a safeguard to see that the general policy of the business is observed with regard to the size of the staff, the scales of wages paid and general working conditions.

A very important part of the work of the Staff Department is connected with training and recruitment. It will be the aim of the department to provide a supply of suitable recruits for vacancies on the selling staff. For this purpose a record of all desirable applicants should be made so that they may be called up at any time in the future if a vacancy occurs for which they are fitted. When suitable persons have been selected in this way they cannot be left



to their own devices to "pick up the business," especially in the case of young people. They must receive a systematic course of training, partly in the business itself and partly in outside educational institutions. Thus, in every business, there are certain matters of internal organisation and routine which are peculiar to that concern and the newcomer must be acquainted with them. In addition, however, if he is to discharge his duties efficiently he will require knowledge of another type—of the commodities he is handling, of business organisation and routine, commercial mathematics, and so on. This may be gained by attendance at outside classes. In either case, the Staff Department will supervise the matter and record the progress which is made and such considerations are bound to play a part when the question of promotion is raised.

(3) **Maintenance and Service.** Under this heading we have the section of the business which is concerned with the maintenance of the store properties and of all the services rendered to the customers. In a large business the upkeep of the premises is a task of some magnitude. The repairs and alterations are continually taking place, whilst fixtures, fittings and equipment have to be constantly inspected to see that they are kept in proper condition. Again, such items of equipment as lifts, fire-fighting appliances, electrical equipment, and ventilating plant depend for their efficiency upon regular inspection and neglect may endanger not merely property, but human life. A large business will, therefore, employ a skeleton staff of artisans to look after these matters, and this staff will be supplemented from outside when larger repairs or alterations have to be undertaken.

In this section also we have the organisation for the packing and delivery of goods to customers, which often assumes considerable dimensions. One of the features of departmental store service to customers is that of the free delivery of goods, and this delivery may be made either in the firm's own vehicles or by an outside carrier. At the present day most large firms maintain their own fleets of motor vehicles for short range deliveries, and rely upon outside transport services only for work which cannot be performed economically by themselves. Delivery in a firm's own vehicles possesses a certain advertising value to the business whilst, if properly organised, it can confer the advantages of greater convenience and safety. Parcels which have to be entrusted to an



outside carrier must be strongly packed to avoid any possibility of damage, but when they are delivered by the firms's own servants, such elaborate packing is not necessary. The delivery organisation must make arrangements for the collection of goods from the showrooms and see that the dispatch instructions issued by the salesmen are duly carried into effect. The manager in charge of the section must schedule his deliveries in such a way that the vehicles under his control are used in the most economic manner, and at the same time he must maintain a proper standard of service.

(4) **Advertising.** The departmental store has always made an extensive use of advertising for the purpose of attracting customers, and developments of recent years have tended to extend these activities. The advertising section must work in close collaboration with the merchandising departments, whilst at the same time there must be co-ordination between all the forms of publicity employed. A certain appropriation will be allocated to the department each financial year, and this must be distributed over the various advertising media so as to secure the best results. Extensive use will probably be made of Press advertising, but this will be supplemented by direct mail advertising in the form of catalogues and price lists. Advertising by means of car bills and posters will also be employed to a varying extent, particularly at sale time, or at special seasons, such as Christmas and Easter. Press advertising may be used in two ways. It may take the form of "house" advertising which is simply designed to keep the name of the firm before the mind of the public. An example of advertising of this type is the column taken by Selfridge & Co., Ltd., every day in *The Times* which is devoted to general topics. On the other hand, such advertising may be "specific" in character, and advertise certain definite lines of goods.

In close association with the advertising activity is the display section which attends to window and shop display generally. This work has assumed special importance of recent years and has become a specialised occupation in a big business. It must be remembered that although advertising may draw customers to the shop, it will not always induce them to come inside and make purchases. If, however, Press or other advertising is supported by an effective display of the actual goods, sales may be made. The aim of the display section will be to create the right "atmosphere" at different



periods according to the season, and give prominence to selected types of merchandise.

(5) **Accounting and Finance.** In view of the complexity of the operations and the large capital involved, the control of the finances of the undertaking is a very important matter. The first requisite is to have an effective system of cash control, the object being to provide that all cash received shall pass into the hands of the cashiers as quickly as possible and be recorded at once. Under most systems of cash control, each salesman makes a summary of his sales which can be compared with the summary submitted by each departmental cashier. In certain cases, where it is not desired that the sales people shall handle cash, customers are requested to pay at conveniently situated cash desks. This plan may be of service in certain cases, as, for instance, when goods have to be packed by the assistant, and this can be done whilst payment is being made. Customers are, however, apt to resent the procedure and, in addition, special safeguards have to be devised to prevent evasion of payment.

The Accounting Section will also be in charge of the ledger accounts, and, since the average departmental store does an extensive business on a credit basis, the amount of work entailed is usually considerable. Most of the large departmental stores have adopted mechanical methods in their book-keeping section in order to cope with the volume of work. This is also rendered necessary by the elaborate analysis of the figures of sales, expenses, and so on, which is required for the purposes of effective financial control. In this connection the large departmental stores have, in recent years, made an increasing use of systems of *Budgetary Control*, i.e. a deliberate planning of expenses in relation to turnover during a trading period, instead of relying merely upon the financial accounts which give information which is retrospective in character. The starting point is the construction of a merchandise budget which must be drawn up for three or six months in advance, estimating the probable monthly sales and gross margins. This work is best performed by a committee consisting of the principal executive officers of the concern. Each item of expense must be considered in relation to estimated sales, and, where necessary, subsidiary estimates will be prepared by managers in charge of spending departments.



# EXPENSE BUDGET FOR THE SIX MONTHS ENDING 31st JULY, 1935

Classification	Complete Period (26 Weeks)				February (4 Weeks)				March (5 Weeks)			
	Estimated	Actual	Estimated	Actual	Estimated	Actual	Estimated	Actual	Estimated	Actual	Estimated	Actual
	£	£	%	%	£	£	%	%	£	£	%	%
Net Sales . . . . .	300,000				40,000	38,900	30-0	1-88	55,000	750	1-36	
Gross Margin . . . . .	90,000				12,000	11,670	30-0	-25	16,500	100	-18	
<b>I. ADMINISTRATIVE EXPENSES</b>												
Executive Salaries . . . . .	4,500		1-5		750	750	1-88	1-25	750	160	1-05	
Bad Debts . . . . .	600		-2		100	100	-25	1-12	580	225	-41	
Audit and Accountancy . . . . .	3,000		1-0		450	475	1-12	-44	225	50	-09	
Stationery, Postage and Telephones . . . . .	1,200		-4		175	197	-44	-13	50	300	-55	
Insurance . . . . .	300		-1		50	50	-12	-07	50	350	-64	
Legal and Professional Service . . . . .	1,300		-1		50	27	-12	-68	300	240	-61	
Clerical and General Wages . . . . .	1,500		-5		240	265	-60	-82	350	2,405	4-37	
Miscellaneous . . . . .	2,100		-7		330	240	-82			1,160	2-11	
<b>II. OCCUPANCY</b>												
Rent . . . . .	13,500		4-5		2,145	2,104	5-35	2-24	2,405	580	1-05	
Rates . . . . .	6,000		2-0		900	900	2-24	1-17	1,160	300	-55	
Heat, Light, Power and Water . . . . .	3,000		1-0		450	450	1-12	-65	300	300	-55	
Maintenance and Repairs . . . . .	1,500		-5		240	250	-60	-61	300	300	-55	
Depreciation . . . . .	1,500		-5		240	240	-60		300	3,220	5-86	
Cleaning . . . . .	1,500		-5		240	240	-60		300	2,000	3-64	
<b>III. PUBLICITY</b>												
Advertising . . . . .	16,500		5-5		2,520	2,530	6-28	4-81	3,220	1,010	1-83	
Display . . . . .	10,500		3-5		1,590	1,600	3-96	2-13	2,000	110	-20	
<b>IV. MERCHANDISING</b>												
Buyers . . . . .	1,500		-5		240	250	-60	-23	300	3,480	6-33	
Receiving and Marking . . . . .	12,000		4-0		1,830	1,850	4-56	7-00	2,300	4,600	8-36	
Selling Staff . . . . .	5,400		1-8		810	820	2-01	9-36	1,010	110	-20	
<b>V. DISPATCH</b>												
Packing and Wrapping Materials . . . . .	600		-2		90	90	-22	-48	110	300	-55	
Delivery Charges . . . . .	3,900		1-3		585	580	1-45	2-32	730	1,140	2-08	
Dispatch Room and Packers . . . . .	1,500		-5		240	240	-60		300			
	6,000		2-0		915	910	2-27		1,140			

Note. This statement will be continued to show the details for each month.



The budget so framed must be elastic, and each succeeding month's estimates will probably require amendment in the light of experience. Thus, an over-spending of advertising allocation would probably mean a reduction in future months. Each month's results must be carefully compared with estimates if full value is to be extracted from the system. Such a system does not operate mechanically, and the personal control of the officials in charge is essential if the best results are to be obtained. The table on page 318 gives a specimen of a typical budget, the actual results for each month and for the half-year being inserted in the columns provided for comparison.

**LIMITATIONS OF THE DEPARTMENTAL STORE.** In all parts of the world the departmental store is now being subjected to pressure by other forms of retail organisations which have developed during the last few years. Among its defects may be mentioned the following—

(1) Over-development, for competitive reasons, of expensive customer-services and excessive advertising costs.

(2) Too many departments and merchandising units, combined with too wide a range of merchandise.

(3) Low productivity in comparison with newer types of distribution, reflected in low volume of business per employee or per square foot of space.

(4) Over-development of mail order facilities in view of the falling off in this type of business.

The very variety of merchandise which has to be stocked is often a source of potential weakness, especially during a period of falling prices. Although the leading stores have taken active steps in the last few years to reduce unnecessary price ranges and variations in quality and style, the ordinary multiple shop, which concentrates its attention on a narrower field, has a much easier merchandising problem to solve. Further, the departmental store is no longer the only retail organisation which enjoys the advantages of large-scale buying, and while the individual department may still retain its supremacy in that direction over the ordinary retail shop, it can no longer hope to compete in mere purchasing power alone with the large multiple organisations.



## TEST PAPER XXVII

1. When and why did *Departmental* Stores first come into existence?
2. Show how responsibility is delegated in the case of a *Departmental* Store.
3. Describe any large Household Stores with which you are acquainted, and point out the chief features of its organisation.
4. What are the chief reasons which attract customers to the *Departmental* Stores?
5. A retail trader gives you the following information concerning his three principal departments—

Average Stock at Cost Price	Annual Turnover	Percentage Mark-up on Cost Price (to Determine Retail Selling Price)
Department A, £500	8	33½
„ B, £1,500	4½	50
„ C, £480	2½	60

Find (a) his gross profit for the year, (b) his average annual turnover. (*R.S.A.*)

6. The cost of doing business (measured as a percentage of turnover) is greater in the case of large departmental stores than in the case of small specialised shops. Why should this be so, and what bearing has this on the future development in retail trade?

7. What are the conditions which would appear to be essential to the success of departmental stores? Describe a suitable form of organisation for a departmental store with four selling departments.

8. The Ever Ready Retail Departmental Store Co., Ltd., finding that they are not making the headway expected, decided to appoint you as manager so that you can make a thorough investigation of their business and methods with a view to developing an up-to-date system for operating their business. Describe briefly the lines upon which you would proceed with investigation and outline the type of costing system you would suggest, noting that the proprietors wish weekly statements showing the following—

- (a) Value of weekly sales at cost.
- (b) Value of sales by department at cost.
- (c) Value of sales by individual salesmen at cost.
- (d) Oncost expenses classified.

9. The following is an extract from the statistical report of a large retail departmental store—

Average Stock at Cost	Annual Stock Turn	Margin of Gross Profit	Expenses
Furniture Dept., £1,500	3	30	25
Ironmongery „ £1,000	5	25	20
Grocery „ £2,000	10	20	16

(Margin of gross profit and expenses are percentage of turnover.)

Find the total gross and net profits earned by the three departments. Find also the average cost of conducting the business.



## CHAPTER XXVIII

### THE MULTIPLE SHOP SYSTEM

**GENERAL CHARACTERISTICS.**—A multiple shop or “chain store” system may be defined as a system of branch shops operated under a centralised management and dealing in similar lines of goods. Apart from this general characteristic the details of the organisation and management of individual businesses vary widely. As already indicated in the general survey of retailing organisations, the multiple shop system is the natural product of business expansion when extension requires the multiplication of selling points rather than the expansion of existing premises. For this reason we can find all over the country embryo multiple shop systems, a few of which may ultimately expand into regional or even national chains, though the great majority are likely to expand to a certain point and then stop. The reason for this is not far to seek. In the case of most businesses which are developing, there arrives a critical period when, if further expansion is to take place, a drastic re-orientation of method becomes necessary. Furthermore, even if that re-organisation were to be effected, it by no means follows that the man who can efficiently manage half a dozen shops will possess the capacities needed for running twenty. In consequence, therefore, expansions of this type tend to go so far and then stop, and the typical problems associated with chain store organisation and management do not arise.

The urge towards the formation of trading systems of this type is not confined merely to the retail end of the distributive system, for we also have a number of multiple shop systems which have been created by manufacturers. In many lines of industry manufacturers have explored the possibilities of producing goods cheaply on mass production lines, but have failed to find a satisfactory market through existing trade channels. In order to provide an outlet for their goods they have set themselves to gain control of a system of retail shops, either by opening new shops in selected neighbourhoods, or by securing the control over shops already in existence. A similar policy may have been pursued with a view to



diverting to themselves the middleman's profit, but this aspect of the matter will be discussed in a later chapter. Now, inasmuch as such a policy would involve the manufacturer in a close consideration of retail problems he will stand a greater chance of success if he can limit the number of his retail outlets consistent with obtaining that efficiency of distribution which he is seeking. He will, therefore, stand a good chance of success if he is dealing in what are sometimes described as "shopping lines," i.e. consumers' goods of a relatively durable type which are purchased at infrequent intervals usually at a recognised shopping centre, such as boots and shoes, or clothing. Again, if the article being sold is such as to require that expert advice and assistance shall be given to the consumer when making the purchase, it may prove more satisfactory to the manufacturer if sales take place through his own shops where assistants can receive the requisite degree of training to give this service. Furthermore, by developing a multiple shop system of distribution, a manufacturer may consolidate his hold upon a particular market and make it difficult for competitors to obtain a footing. If distribution is made through independent retailers, these may be won over by a new competitor, but where distribution is through the manufacturer's own shops this difficulty does not arise. Unless some of these considerations apply this method of distribution may prove unsatisfactory to the manufacturer.

**CLASSES OF GOODS.**—A further question arises as to the types of products which are most suitably handled by a multiple shop system. In this connection it is impossible to be dogmatic, for this system of distribution has been applied to one set of products after another in recent years with the result that it would almost appear that, given the right management and methods, almost any type of product can be handled. None the less it is possible to lay down certain wide considerations which influence the suitability of a product for this class of business.

(1) The articles should be of such a type that a *rapid turnover* may be expected. The expenses of multiple shop operation are considerable, both on account of the centralisation of management and control, and also because of the high rents which are paid by branches in order to secure the most suitable sites. Hence, these overhead charges must be spread over a big turnover in order to keep selling prices down to a minimum. The need for a large turnover is



intensified by the fact that in many cases the multiple shops appeal to their clients on the score of cheapness and, therefore, fix their selling prices at a lower level than their competitors.

(2) In order to achieve the first objective, the commodities handled should be *necessities* or semi-necessities which are in constant demand. Thus, foodstuffs, articles of clothing and footwear are commonly dealt in by the multiple shops, though perishable foodstuffs are not frequently handled by this system of distribution, probably owing to the difficulties of applying a centralised system of purchasing and stock control to them. The multiples have a further inducement to deal in necessities in the fact that the demand for such commodities is relatively steady and may therefore be more readily predicted. The consumer demand for fashion goods is essentially capricious, so that a multiple shop system which handled such goods would be exposed to very serious risks for which the possibility of large profits would be no adequate compensation.

(3) Generally speaking, the article should be of the standardised *branded type* requiring little selling effort on the part of assistants. In spite of what has been said above with regard to the establishment of multiple shop systems by manufacturers for the purpose of providing specialised selling services, a large part of multiple shop selling is of a routine character. This applies particularly to the fixed price multiples of the Woolworth or Marks & Spencer type, where the function of the assistant is mainly to pack the goods and take the cash from the customer. Of recent years, many of the larger multiples have inaugurated schemes of staff training with a view to improving the capabilities of their assistants, but the difficulties encountered in a large organisation are considerable.

(4) The territory served by the branches should be one in which the units are not too far apart to permit of *effective supervision and supply* from centrally located warehouses. Since centralised buying is one of the advantages enjoyed by multiples, individual branches should not be separated by great distances, otherwise this advantage will be lost by heavy costs of carriage. In the case of national multiple shop systems the same rule applies, but the organisation may be divided on a district basis for administrative purposes.

(5) In view of the fact that multiple shops usually aim at reducing auxiliary selling services to a minimum, the articles sold should be of a *portable type* which are usually purchased in small amounts so



that customers may easily carry them away. In this way the cost of free delivery services is saved.

**PRINCIPLES OF MULTIPLE SHOP OPERATION.**—The multiple shop system came into being as the result of an effort to provide a system for the efficient distribution of consumers' goods in the large quantities warranted by modern production. The success which has crowned the efforts of many firms engaged in this class of business has led many to believe that it is due to certain factors which are beyond the reach of the small retailing concern. It has been stated that the economies of "mass distribution" are analogous to those of "mass production" which have long been familiar to students of economics, and that in either of them the small business can have no share. Recent events, however, have shown the falsity of the easy acceptance of such a point of view. There is nothing inherent in large-scale operations, either in the sphere of production or of marketing, which makes them naturally more efficient or economical than small-scale. Over-credulence on this point has led to many misfortunes in business in recent years.

The multiple shop system is faced with the problem of reconciling two principles—the *centralisation* of buying and administration with the *decentralisation* of selling through a large number of branches. In the first place, it will have to be decided how far this centralisation of administration is to be carried; in other words, how much power is it advisable to delegate to branch managers. A branch manager may have so little discretion allowed to him that he sinks to the level of a senior shop assistant, with the result that the whole system is liable to become bureaucratic and lose in efficiency through inelasticity. On the other hand, if branch managers are given too much latitude, the organisation may get beyond proper control. The secret of successful organisation will be to strike the happy medium and, in any case, clearly to define the limits of authority delegated to the local management.

Again, the multiple shop system operates on the principle of making centralised purchases, pooling the requirements of the whole system, and buying in bulk. In the case of standardised branded goods which are in widespread demand, this policy is sound, but in any line of business where there is scope for the action of local prejudices it may be opened to criticism. In the case of certain types of goods which may be stocked by branches it may, therefore, be expedient



to adopt some measure of decentralisation and allow managers discretion, within limits, as to the goods which they will stock. Such a course is adopted for example by Messrs. W. H. Smith & Son, Ltd., where in certain of the branches the manager has power to satisfy his requirements locally for some lines of goods. Again, the Times Furnishing Co., Ltd., allows its branch managers to satisfy their own requirements, but the head office management decides the firms from which purchases shall be made. Such a system throws a great deal of responsibility upon the local manager, who must forecast what lines are likely to be in demand by his customers.

The decentralised selling activities of the multiple shop system call for special organisation in such matters as cash and stock control. Unless a careful and systematic check is kept over branches in respect of these matters an avenue to heavy losses is opened up. Special arrangements have to be made for invoicing goods to branches, a common arrangement being to invoice them at the retail selling price since this facilitates stock control. The branch manager then has to account for a certain value of goods sent to him, and the amount of his sales together with the value of his stocks at any time should correspond with the value of goods invoiced. Cash takings have usually to be paid into the local bank to the credit of Head Office Account at frequent intervals, and a return made either day by day or at the end of each week.

The success which has attended multiple shop operation has been largely due to the close attention which the majority of these organisations have paid to certain aspects of retail business practice which are often neglected by the small independent retailer. To these we shall now turn our attention—

(1) **Accounting.** One of the factors in favour of the multiple shop system is the close attention which is paid to accounting and statistical records. It was pointed out by the Linlithgow Committee on the Distribution and Prices of Agricultural Produce that very few small traders keep accounts in such a way as to show the relationship of the constituent elements in the costs of their respective undertakings. Now a trader who fails to keep proper accounts can exercise no adequate control over the various items of cost which are incurred in the course of his operations. He cannot compare his expenses now with those of previous periods, nor can he compare his experience with that of businesses of a similar type.



The multiple shop system, in its very nature, cannot afford to allow any items of expenditure to pass beyond effective supervision, and has consequently devoted considerable effort to the development of a technique of statistical and accounting control which is capable of shedding light on all the manifold activities of the business. Undue increases in expenditure are immediately revealed and eliminated, whilst the experience of one branch can be compared with that of another, and a close check kept upon the efficiency of every unit in the organisation.

(2) **Advertising.** The second advantage which the multiple shop system enjoys is the attention which it can devote to problems of advertising. In the first place it can afford to employ specialists either on its own staff or through recognised advertising agencies—a course of action which is quite beyond the means of the small independent retailer. Two methods of approach are possible in dealing with multiple shop advertising, viz. the appeal may be centred on the goods themselves or, alternatively, some form of institutional advertising may be adopted, i.e. attention is concentrated upon the firm which is selling the merchandise. As a general rule, in the case of a national multiple shop system some form of national advertising will be adopted. In addition, however, it will usually be found beneficial to undertake a certain amount of advertising into which local colour and appeal is introduced. In this way something of the personal touch which characterises the independent retail business is introduced.

(3) **Purchasing.** The requirements of a multiple shop system for merchandise are larger than those of many wholesale firms, so that it is possible for such an organisation to go back to the original sources of supply and purchase its requirements on the best possible terms. Moreover, since this work of buying is performed by experts the chances of the goods proving acceptable to the buying public are increased. The reduced prices at which multiple shop systems can purchase the goods which they stock may arise from a number of causes. In the first place, the organisation can go direct to the manufacturer and, in consultation with him, plan and produce those articles which are in most active request at the time at a price which ensures a steady demand. The large orders which can be placed enable the manufacturer to produce continuously and to utilise mass production machinery. Apart from such savings in



the physical production of goods, economies are also made in their sale. The multiple shop organisation being in direct contact with the manufacturer enables him to dispense with travellers, wholesale houses, and other intermediaries, and all these savings are reflected in the price at which the merchandise is bought. In some cases, multiple shop systems which have been established as purely distributive organisations have taken over the ownership of manufacturing businesses in the hope of achieving further economies in this direction. Such a course of action contains a considerable element of risk, since the shops may sooner or later find themselves compelled to stock articles from their own factory which could be bought more cheaply elsewhere.

(4) **Business Location.** The location of a business enterprise, particularly in the retail trade, is one of the most important determinants of success. In this respect the small retailer is at a disadvantage, because even in those infrequent cases where he has the ability to judge the merits of a site, he rarely possesses the capital to enable him to acquire it. The multiple shop company, on the other hand, will usually have a special estate department which can not only investigate sites for opening new branches, but also watch developments in connection with existing branches. Indeed, the movement of shopping centres is a factor of immense importance to the retail trade. The development of housing schemes creates new centres of population, whilst the decline of certain industrial centres destroys what were once good retailing centres. These developments can be followed closely by the multiple shop companies, and, on account of their capital resources, these concerns can take advantage of the information which they collect.

(5) **Specialisation.** The principle of specialisation may be said to be applied in two ways in a multiple shop system, viz. in regard to the merchandise and in respect of the staff. In the first place, the majority of multiple shop companies specialise in handling a limited number of lines, e.g. meat, dairy produce, or groceries, thereby leading to a simplification of retailing methods and equipment. Secondly, on account of the large scale of the operations and the attempts made at centralisation of business control, scope is offered for the specialisation of personnel. Thus, as we have already seen, expert buying agents can be employed to purchase merchandise for the whole organisation; accounting and statistical records can

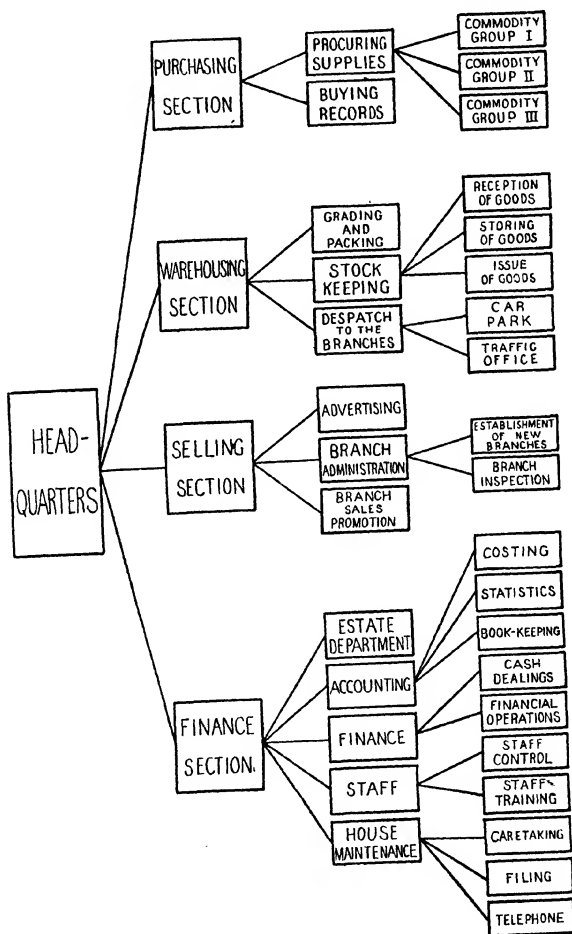


be compiled under the supervision of experienced accountants, whilst the management of the business premises devolves upon the estate manager. On the side of publicity, experienced advertising experts may be employed, whilst specialist advice can be given to individual branch managers on such matters as window display and the arrangement of stock. In a smaller concern, these matters have usually to be dealt with by one man who, no matter how great his ability may be, cannot hope to deal efficiently with them all.

**ORGANISATION OF A MULTIPLE SHOP BUSINESS.**—The multiple shop business is an attempt to reconcile a centralisation of administration with decentralised selling, and many of the special problems of such a system arise on this account. The central administration of the whole enterprise will be found at the head office, where, in a large organisation at all events, four sections may be recognised—Purchasing, Warehousing, Selling, and Finance. The *Purchasing Department* is, of course, a very important section of head office organisation, since the policy of the multiple shop is to pool the requirements of its branches and to buy in bulk. The demands made upon the concern often necessitate going out into the world's markets and purchasing in large quantities as well as in advance of actual requirements. In order to supply branches with the newest styles and latest discoveries it is essential that all sources of information be tapped. The fact that a large proportion of the capital of a multiple shop company is invested in stock constitutes its greatest weakness or strength according to the measure of skill exercised in the buying. The exact organisation and policy of this department will depend partly upon the size of the business, and partly upon the type and range of articles which are regularly stocked by the branches. Moreover, further modification will take place if the business manufactures some or all of its requirements in its own works. When purchases are made goods will be sent direct to the branches whenever this is possible, but usually it will prove necessary to maintain warehouses for holding reserve stocks and in order to make bulk purchasing possible. The *Warehouse* may be situated on the same premises as the head office, or a policy of decentralisation may be followed by locating branch warehouses in the areas which they are expected to serve. Again, different warehouses may be employed for different classes of goods where special conditions of storage are called for.



# SCHEME OF ORGANISATION OF A LARGE MULTIPLE SHOP CONCERN





**BRANCH WEEKLY CASH RETURN**  
THIS CASH RETURN MUST REACH HEAD  
OFFICE FIRST POST MONDAY MORNING

Week Ending.....29/10/3.....

Branch Stamp.

THE MULTIPLE SHOP CO., LTD.,  
84 ST. JOHN'S SQUARE,  
CARDIFF.

Tel. No.....Cardiff 186....

DATE	CASH RECEIPTS						CASH PAYMENTS									
	Cash Sales			Credit Accounts Paid (Net Cash Rec'd)			Total	Particulars	Total							
	£	s.	d.	£	s.	d.			£	s.	d.					
Monday	14	18	7	32	2	2	47	0	9	Gross Wages per Wages Sheet		18	9	0		
Tuesday	18	6	1	1	8	9	19	14	10	Traveller's Commission						
Wednesday	9	2	3	-	-	-	9	2	3	Sick Pay per Wages Sheet						
Thursday	31	2	9	11	10	10	42	13	7	Insurance Stamps (Company's proportion)			12	3		
Friday	59	5	2		18	7	60	3	9	Carriage In						
Saturday	73	17	0	2	6	0	76	3	0	Bike Repair						
Cash Credit Notes	-	-	-							Oil						
Total	206	11	10	48	6	4	254	18	2	Local Delivery						
Club:										Van Hire	10	0				
Stock brought forward				10	16	3					10	10				
Received during week				12	10	0				Postage and Telegrams			3	3		
Total				23	6	3				Weights Adjustment				1	10	
Less Stock on hand				20	14	3				Scales, Bacon Machines, Sharpening Saws, etc.						
Stamps issued				-	-	-	2	12	0	Sundry Expenses—give details						
Sub-Tenant's Rent										Tacks 3d. Dust . 1/6		1	9	1	9	
										Special Items						
Pension Fund																
										Total						
										Club Withdrawals			1	13	0	
Total Cash Received for other Branches—										Local Purchases as per Sheet attached						
Date	Branch	Customer's Name								Relief Vouchers sent to H.O. for Collection						
										Cash Credit Notes (Nos.)						
										BANKINGS						
										Tuesday	47	0	9			
										Wednesday	19	14	10			
										Thursday	9	2	3			
										Friday	42	13	7			
										Saturday	40	3	9			
Other Receipts—give details										Balance to be Banked Monday	77	3	1	235	18	3
														257	10	2
							257	10	2							

.....John Strong.....  
Branch Manager.



A number of different systems of supplying branches with stocks are employed, but generally speaking responsibility for maintaining stocks may rest either with the head office or with the branch managers. From the standpoint of effective control the former system is probably the more efficient. The branch managers make weekly returns of stock movements, and upon the basis of these returns the Branch Supplies Department at head office can determine the requirements of each branch, and instruct the warehouse to make such deliveries as are considered necessary. In this way over-stocking as a result of mistakes of the branch management is avoided, and a uniform policy can be followed in respect of all branches. For the purpose of the delivery of goods from warehouse to branches, the multiple shop may maintain its own transport department. Where a company has its own transport, a definite rota of deliveries should be arranged. The transport department should so arrange deliveries as to ensure that the branches are adequately stocked. Where deliveries to customers have to be made (e.g. bread) light vans or carrier cycles may be used.

In many of its aspects the *Finance Section* of the head office will not differ from that of other large business. If, as is usually the case, the business is organised as a joint stock company, there will be a Secretary's Department dealing with the routine matters of company work. The Accounting Section deals with the financial records, although in this case comprehensive statistical records will be necessary for the purpose of comparing the results of one branch with those of another. This department will also deal with the various returns which have to be made by the managers of each branch. The most important of these is the *Weekly Stock Report*, which, as shown in the example on page 332, gives details of—

- (a) Opening stock of each line of goods.
- (b) Deliveries received during the week.
- (c) Balance on hand at the end of the week.
- (d) Sales for the week, i.e.  $(a) + (b) - (c)$ .

In addition to this return, which is concerned mainly with quantities, a *Weekly Cash Return* on the lines illustrated on page 330 must also be submitted. This return can be simplified considerably if cash sales only are made, but if credit transactions are allowed details must be furnished to the head office on the lines indicated.\*

Another important section of head office organisation as already



**THE MULTIPLE SHOP COMPANY, LTD.  
WEEKLY STOCK REPORT**

To HEAD OFFICE.				
From..... <i>Cardiff</i> .....Branch.				
Week ended..... <i>17th Nov</i> ..... <i>19</i> ..				
Particulars	Stock Monday Morning	Received during Week	Stock Saturday Night	Sales
*	£   s.   d. 927   5   9	£   s.   d. 329   11   0	£   s.   d. 991   10   1	£   s.   d. 265   6   8

indicated will be the *Estate Department*. A multiple shop company has to manage a large amount of property and must, moreover, be constantly adapting itself to changing circumstances. It must open new branches in areas which are developing and, if necessary, close them in other areas where they can no longer be made to pay. Hence, it pays the multiple shop to employ the full time services of an expert Estate Manager who can safeguard its interests in this connection.

On the sales side of the multiple shop business, a staff of specialists will be maintained at head office for the purpose of organising the control of the branches and for keeping the management in touch with local conditions. General advertising, window display, and similar matters will be directed from head office so that a co-ordinated policy is initiated for the whole organisation. The head office is brought into touch with the branches through the medium of a District Manager or Inspector who is responsible for the conduct of the branches in his area. These officials have to check the stocks of the branches and make an independent verification of other details in the returns supplied to head office in the course of their periodical visits. The greater the degree of independence allowed to the branches, the more important and onerous do these duties become.

**TIED SHOP.**—A form of retail trade closely allied to the multiple-shop type is carried on in undertakings acting as agencies, and often “tied” to some large firm. The most common example of this kind



is the "tied" house in the licensed victuallers' trade, where a brewery controls a chain of public-houses devoted solely to the sale of its products. In a certain measure the same custom prevails in the tobacco and jewellery business. In the latter trade the stock is all supplied on credit, and though ostensibly the business is independent, in reality such independence is entirely fictitious; the jeweller is simply a salesman on commission and the business may be described as a "tied shop."

### TEST PAPER XXVIII

1. What is meant by the Multiple Shop System?
2. Contrast and compare the Multiple Shop System and the Departmental Store.
3. "The Multiple Shop System is an attempt to eliminate the profits of the middleman." Explain this statement.
4. In the case of the Multiple Shop System, is it always advisable to supply the shops from *one* central depot? If not, why not?
5. Enumerate some of the chief advantages of distributing goods through a system of Multiple Shops.
6. Compare and contrast the features of a large-scale multiple shop business with those of a large-scale departmental store business.
7. What are the chief advantages possessed by a retail shop conducted by its owner over a retail shop forming one of a group of multiple shops? Under what circumstances is the latter the more successful form of business?
8. "A proportional application of the principles of centralisation and decentralisation is the secret of successful organisation in a system of multiple shops." Expand this statement and discuss its significance.
9. How far, in your opinion, does the multiple shop system in retail trade lead to standardisation, simplification, and specialisation in the details of the business carried on?
10. A limited company carrying on business as gentlemen's outfitters has a factory and central warehouse and a number of retail establishments situated in different towns. The head office supplies the branches with all goods. Your advice is sought as to the best method to be adopted for the purpose of charging out goods supplied to the branches, and allocating between them the following items of expenditure—  
 Advertising manager's salary.  
 Cost of advertising.  
 Service of motor vans.  
 Give your answer in the form of a report to the directors.
11. Mr. T. Jones is South Wales District sales manager for Robinson & Brown, Ltd., Wholesale Clothing Manufacturers, 54 Oxford Street, Manchester. Draft a copy of his report to Head Office for the week ended 30th June last, embodying the following points and any others which suggest themselves to you—  
 (a) Retail business is quiet following the sales rush at Whitsun, but is expected to improve during July.  
 (b) Retailers inquiring for quantities of low priced goods for July "sales."  
 (c) Serious complaint from one firm regarding delayed deliveries.
12. What is meant by a "tied shop"? Give an example.



## CHAPTER XXIX

### DISTRIBUTIVE CO-OPERATION

A CO-OPERATIVE distributive society is a combination of persons whose aim is to economise by buying in common and to retain their profits by selling in common. These societies were, to a great extent, a consequence of the Industrial Revolution, which led to the creation of a large permanent working-class, who organised themselves as wage-spenders in the co-operative stores. The movement has flourished chiefly in Lancashire, Yorkshire, the Midlands, and in the Valley of the Clyde; in short, in those districts where trade unionism has been most successful. It seems to have met with but limited success in large seaside towns with moving populations; among the very poor, who cannot always afford to pay ready-money for their purchases; and among the very rich, who desire greater time and attention bestowed upon them when making their purchases.

**CHARACTERISTICS OF A CO-OPERATIVE SOCIETY.**—The distributive societies of the present day are based on the plan of the famous Rochdale Equitable Pioneers' Society, founded in 1844. The founders of this Society, recognising that every producer is also a consumer, aimed at providing for the needs of their members in both of these capacities. The first object of the Pioneers was "the establishment of a store for the sale of provisions, clothing, etc.," but ultimately they considered that "this society shall proceed to arrange the powers of production, distribution, education, and government; or, in other words, to establish a self-supporting home colony of united interests, or to assist other societies in establishing such colonies." Now, one of the great difficulties experienced by the average business engaged in distribution is that of ensuring regularity of demand. From the outset, however, the co-operative stores adopted a device in the form of a dividend upon purchases that ensured such a demand. Under the Rochdale plan, the shareholders got 5 per cent interest on their capital, while the customers got the remainder of the surplus of sale receipts over purchase price plus overhead charges, and what the customers got was treated as a rebate, and was not regarded as a profit made by the vendor



society. After a time, however, there was a departure from the rule originally followed, and by setting aside a larger portion of their surpluses than was essential for normal reserve fund purposes, the societies were able not only to expand their operations on modern competitive lines by opening new shops and purchasing established businesses outright, but also to subscribe to the capital of the whole-sale societies.

Co-operative societies are governed by the provisions of the Industrial and Provident Societies Acts, 1893–1928. They possess the following characteristics—

(1) **Open Membership.** Membership is open to all comers, the committee of the society, however, usually having the right to refuse the admission of any person whose membership is regarded as likely to be detrimental to the interest of the society. In this respect the co-operative society differs from the registered company since the membership of the latter is limited by the amount of its nominal capital.

(2) **Democratic Control.** Almost without exception each individual member possesses one vote, irrespective of the number of shares held. Where share capital is owned by other societies, these societies are usually allowed additional votes in some proportion to the amount of share capital held by them. These provisions prevent the domination of societies by groups of large shareholders. In the absence of any disqualifying rule, every person who has been admitted to membership and has had his name added to the list of members is entitled to vote even though his share or shares are not fully paid.

(3) **Provision of Capital.** The shares in a society (which are invariably issued at par value) are in all cases of small amount, usually £1. They may generally be paid up by weekly or quarterly instalments, or by the automatic accumulation of the sums accruing to the holder as his share in the profits of the society without the necessity for any cash payment beyond a trifling amount paid on allotment. A co-operative society can increase the amount of its share capital to any figure it likes, so long as no individual holds a greater amount of shares than £200. The bulk of the share capital is withdrawable at short notice, though many societies compel each member to hold at least one transferable share, which can be realised only by sale.



(4) **Limitation of Interest on Capital.** The return on share capital is in most cases limited to a fixed rate of interest, usually 5 per cent per annum. In some societies the full rate of interest is not paid if the member's purchases fall below a stated amount in a given period.

(5) **Distribution of Surplus.** As already indicated, these are usually distributed among the members in proportion to the amount of each member's purchases. In this respect the practice of the societies is in sharp contrast with that of the joint stock company, where the surplus is distributed as a dividend on share capital.

**THE CO-OPERATIVE RETAIL SOCIETY.**—In accordance with the fundamental assumption in the theory of co-operation that economic organisation should be based upon the supply of consumer's wants, co-operative organisation naturally starts from the consumer. Hence, the foundation of the whole structure of the co-operative movement in this country is the society of purchasing members known as the retail society. It is the members of these retail distributive societies who supply the great bulk of the capital of the movement, and from their number are chosen its administrators and most of its employees. Thus, at the present day there are some 1,150 retail societies with a membership of approximately seven millions. The number of members is continually increasing whilst the number of societies has diminished. When new areas are opened up for co-operative distribution, it is now usually possible for an old-established society, operating within a reasonable distance, to cover the area, so that there is no need to form a new society. Again, in recent years there has been a tendency for the size of the typical business unit within the movement to increase. This process is still continuing fairly rapidly through amalgamation of old-established societies, thereby leading to a reduction in their number.

The first step in the formation of a retail society is to find a number of persons who desire to undertake, in common, those trading operations which have formerly been performed for them by others. In most cases, a certain amount of propaganda will be required in order to obtain a group large enough to form the nucleus of a co-operative society. In order that a society may be registered under the Industrial and Provident Societies Acts, the following conditions must be fulfilled—

- (1) The society must consist of at least seven members.
- (2) It must have a clear identifying name.



- (3) The word "limited" must be the last word of its name.
- (4) No individual member, other than a registered society, shall hold more than £200 in share capital.
- (5) It shall not carry on a banking business if its share capital is withdrawable, unless the same be on deposit of not more than 10s. at a time, no separate depositor holding more than £20 at any one time, his holding being repayable at not less than two days' notice.
- (6) The application for registration shall be signed by seven members and the secretary, and shall be accompanied by two printed copies of the rules for registration.

The rules of the society may embody all such matters as the members may see fit to include, always provided that nothing is embodied in them which is contrary to the provisions of the Acts. To-day, it is unnecessary for societies to draw up their own rules, the Co-operative Union—a federation of co-operative organisations—having compiled a set of model rules which meet all the requirements of the Acts, and which, with the addition of any special rules, are easily adaptable to the requirements of any society. The following matters must be provided for in the rules of every society—

- (1) Objects, name, and registered office of the society.
- (2) Terms of admission of members.
- (3) Mode of holding meetings, rights of voting, and method of altering rules.
- (4) Appointment, removal, and payment of committee and officers.
- (5) The holding of share capital which a member must and may take up.
- (6) Provision for taking loans and deposits together with the conditions governing such transactions.
- (7) Determination whether shares shall be withdrawable or transferable.
- (8) Conditions of withdrawal from the society.
- (9) Mode of application of profits.
- (10) Provision for custody of the society's seal and for its use.
- (11) Provisions regarding investment of capital.

The control, management, and administration of a society are divided among the members, the committee, and the permanent officials of the society, and in this respect the organisation bears a certain resemblance to that of a joint stock company. As a democratic organisation, the control of the society is vested in the members, but at the present day this control is exercised through a committee, and is limited to the approval or criticism of the actions of this body. The committee itself is responsible for the general administration of the society and should, therefore, keep in close touch with the members, whose wishes on all matters of policy should be consulted. For the purpose of economising time and securing greater efficiency, the committee may divide itself into



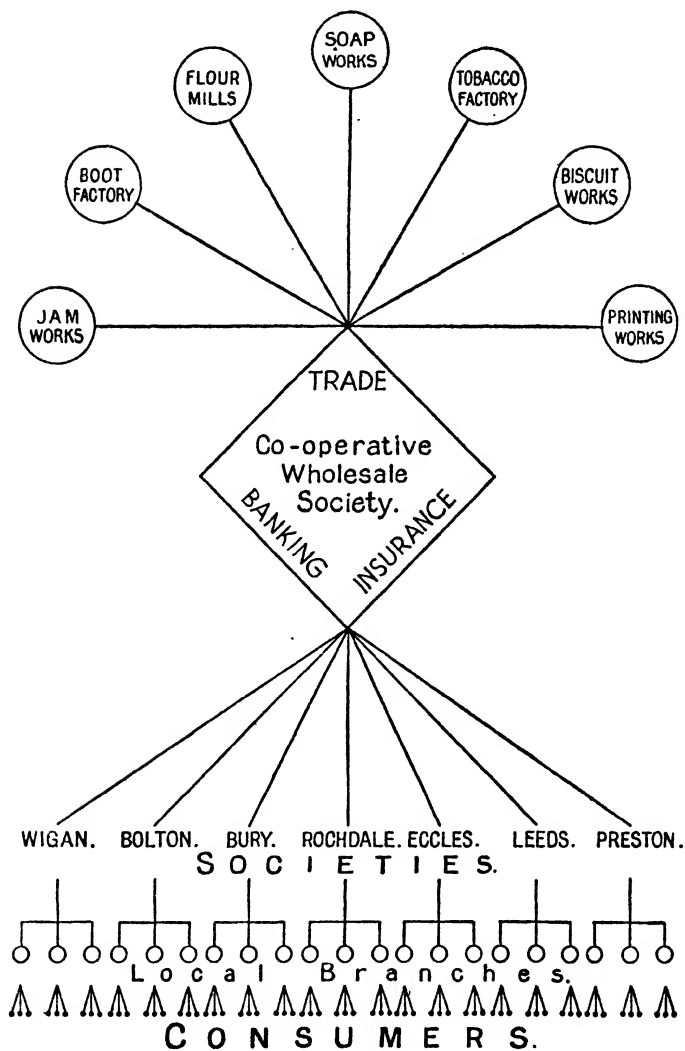
sub-committees to supervise and keep in touch with each department and the manager. Each sub-committee will receive regular reports from the management with regard to the activities of the section of the business with which they are concerned, and upon these they can base their decisions and recommendations.

**Trading Policy of the Retail Societies.** The growth of the co-operative movement has been accompanied by development on the part of its competitors, so that to-day the societies are faced by more intensive competition than at any time in the past. The competitors of the movement, notably the multiple shops and departmental stores, have steadily improved their organisations and their methods of doing business. The multiple shop, for example, as we have already seen is rendered formidable on account of the high degree of specialisation which attends its operations. Multiple shops, selling a limited number of lines of goods, can buy to greater advantage than would be possible were they to stock a wider range. The buyer can watch his markets better and stocks can be kept more easily under control. On the selling side, prices can be varied more promptly to meet changes in market conditions, whilst smaller stocks in relation to turnover are required in the shops so that economies in the use of capital are secured. Furthermore, the competition of these concerns is by no means confined to the large towns, but is found throughout the country in all the lines of goods ordinarily stocked by the co-operative societies.

One of the difficulties of the co-operative retail society arises from the fact that it attempts to run specialised branches in a number of different lines—grocery, butchery, drapery, etc.—and the two do not always blend very well. Again, the multiple shop pays a considerable amount of attention to the external appearance of its premises and the display of its goods, whereas the co-operative society, in many cases relying upon the loyalty of its members, has paid insufficient attention to such matters. In regard to managerial control, too, the large-scale competitors of the co-operative stores have set themselves to perfect systems of accounting and statistical control which enable them to keep in the closest touch with every aspect of business operation. Many societies are backward in this respect and are, therefore, handicapped from the standpoint of competitive efficiency. From the standpoint of control, the government of the societies through a committee imposes



## CO-OPERATIVE DISTRIBUTION





certain disadvantages, usually on account of the fact that committees often take upon themselves duties and responsibilities which they ought to leave to managers and officials. This practice not only delays decisions, but stifles initiative and weakens the sense of responsibility in the officials.

**THE CO-OPERATIVE WHOLESALE SOCIETY.**—The Co-operative Wholesale Society is a federation of societies, the purpose of which is to control for the benefit of all co-operators those stages of manufacture, importation, merchanting, and financing, through which most goods pass before they reach the retail store. The society was first registered in 1863 with the object of doing a certain amount of wholesale buying on behalf of the various new co-operative stores of the northern counties. The early years of its life were full of doubts as to its strength and capacity to live, but it is to-day, with the exception of Centrosoyus, the largest co-operative society in the world. The functions of the Co-operative Wholesale Society can be divided into four parts, namely—

(1) **Wholesaling.** The factoring of goods is probably the most important of the various activities of the society, and accounts for the largest part of its trade. The large variety of goods which the co-operative societies supply to their members has resulted in the Co-operative Wholesale Society having numerous sales departments, from which the buyers of the retail societies can obtain the goods they require. These sales departments are established at three main centres, Manchester, London, and Newcastle; and on a somewhat smaller scale at Bristol, Cardiff, Northampton, Plymouth, Birmingham, Nottingham, Liverpool, and Leeds. Each serves a definite area, and the managers or buyers of the retail societies regularly visit the salerooms at the headquarters of their particular areas to order supplies. Many of the smaller societies are served by Co-operative Wholesale Society travellers, who represent the various departments, and who keep the local retail managers fully informed of changes in trading conditions.

(2) **Importing.** Many of the foodstuffs sold by the Co-operative Wholesale Society are obtained from abroad, so that the society is engaged on a big scale in the business of importing goods. As far as possible, supplies from overseas are obtained from co-operative producers, as in the case of Denmark, where bacon factories and butter depots have been established. In several countries, the



Co-operative Wholesale Society has given direct assistance to the co-operatively organised farmers. Examples of its activities on these lines are its participation in the New Zealand Produce Association, which is jointly owned by the Co-operative Wholesale Society and the New Zealand farmers' co-operative societies to market New Zealand produce in Great Britain; associations with the Canadian and Australian wheat pools; and trade with co-operative fruit growers in Palestine.

(3) **Manufacturing.** The Co-operative Wholesale Society operates some 140 factories and employs over 35,000 workpeople in the production of a wide range of the commodities which it distributes. No other undertaking in the country covers such a wide range of manufactures, and the number is constantly being extended. Co-operative production of this character is, of course, limited by the market offered by the retail societies. It is stated that this market is narrowed by the conservatism of many co-operative consumers, expressed in a preference for old-established proprietary brands of articles, coupled with a marked unwillingness to experiment with co-operatively produced alternatives. The resentment of the British co-operative movement at the additional taxation imposed upon them in 1933 has led to a campaign for the exclusion of goods of a non-co-operative origin from the stores. Again, the development of co-operative productive activities has been stimulated by the refusal of some traders to supply their price-maintained products to co-operative societies, on the ground that the payment of a dividend on purchases is the same thing as the offer of a price rebate.

(4) **Banking and Finance.** Co-operative finance in Great Britain can be divided into two distinct ventures—the Co-operative Wholesale Society Bank and the Co-operative Insurance Society. The Co-operative Wholesale Society Banking Department has headquarters at Manchester, with branches at London, Newcastle, and Bristol, whilst a number of Co-operative Wholesale Society depots and most retail distributive societies in England and Wales transact the simpler banking operations as agents for the department. Over £700,000,000 passes over the counter of the bank in deposits and withdrawals every year. The Co-operative Insurance Society, which is under the joint control of the Co-operative Wholesale Society and the Scottish Co-operative Wholesale Society, conducts all kinds



of commercial insurance business for co-operative societies, whilst the customary life, accident, and property insurance services are provided for individuals.

**RELATION BETWEEN WHOLESALE AND RETAIL SOCIETIES.—**

The diagram on page 339 serves to illustrate the relationship existing between the Wholesale Society and its members (i.e., the retail societies). The movement now engages in retailing, wholesaling, primary production, manufacture, transport, insurance, printing and publishing, and banking. The bank is not generally used by ordinary members. The retail stores keep their deposits in the Co-operative Wholesale Bank, as also do the trade unions. The legal and parliamentary side of co-operation is undertaken by the Co-operative Union, which holds its annual Congress during Whit-week.

It will be seen from the diagram that the Co-operative Wholesale Society is supplied by its own factories and workshops with the vast majority of the commodities which it sells to the retail societies. The profits earned by the Wholesale Society are distributed among its members (i.e. the retail societies) *pro rata* according to the amount of their respective purchases. These latter societies, in turn, divide their profits precisely on the same basis amongst their own members. Thus, a person who is a member of a co-operative store, say, in Bolton, will receive not only a share of the profits actually made in Bolton, but also a share of the profits earned by the Wholesale Society in Manchester.

**PRESENT SIGNIFICANCE OF CO-OPERATIVE DISTRIBUTION.—**

There are many different views as to the significance of the co-operative movement as forming an integral part of the industrial system. These views may be grouped as—

- |              |            |                |
|--------------|------------|----------------|
| 1. Economic. | 2. Social. | 3. Industrial. |
|--------------|------------|----------------|

**Economic Significance.** The aim of the co-operative stores is to enable consumers to get what they want in their own way. With the elimination of the private retailer and wholesaler, there is less risk of the goods being adulterated, or of the inferior but more profitable brands being forced upon the consumers. Another economy is that the co-operators become their own shopkeepers, controllers, auditors, etc.

On the other hand, it has been said that the Stores may keep



the customer waiting to be served, and that the co-operator gets less for his money than at the private shop, where there is a greater selection.

The goods at the Stores are sold at market prices. The advocates of co-operation hold that this method has advantages in that it shows the profits earned under the system in the form of dividend, and it also avoids friction with the private shop-keepers. The question often arises as to whether the dividends paid by the Stores are a measure of their economic superiority over the ordinary retailers. The answer of private traders is that the dividend is a delusion, and that the consumer loses, even after taking the dividend into account, owing to the inferiority of the goods supplied by the Stores. It is further argued that, in order to maintain a high dividend, the Stores charge more than the market price for certain articles.

**Social Significance.** In the first place, the Store is a training ground in self-government, since every member has indirectly a voice in the management. Any person over 18 years may become a member and possess a vote, although each member must hold at least one share in the Society. In many Stores a system of credit has been introduced, but the general rule is still cash payments. Moreover, it is argued that such co-operation encourages thrift and working-class investment, since the dividends might be regarded as a form of sub-conscious saving. Finally, the most important social advantage is the monetary sacrifice made by co-operators for the development of education among their members. Their expenditure has been mainly directed towards the furtherance of three branches of education—

1. General instruction in co-operative principles and history.
2. The establishment of libraries.
3. The provision of recreation (e.g. reading-rooms and excursions).

The British co-operative societies do not devote their funds to political propaganda, as is the case in some of the continental countries, though there is a possibility of their doing so in the near future. In England, it is the social side which, so far, has attracted the great leaders of the movement.

**Industrial Significance.** It was not long before the retail societies had a surplus of capital, and they had either to reject



the savings of the members or to re-invest them. This latter they could do either in the development of co-operation or in outside industrial concerns. The retail societies quickly became producers for all the simplest needs which were to be fulfilled near the place of consumption. As regards the production of other articles, power was given to the central agency—the Wholesale Society. The endeavour of the Wholesale Society has been to produce all those things which appear in the workers' budget, so that its productive operations are now very extensive. It manufactures its own flour, butter, biscuits, sweets, preserves, pickles, cocoa, chocolate, cigars, soap, boots and shoes, clothing, furniture, etc. ; and conducts such operations as banking, milling, printing, and fruit-growing.

### TEST PAPER XXIX

1. What are Co-operative Distributive Societies, and where have they met with the greatest amount of success ?
2. Say what you know of the Rochdale Pioneers.
3. What provisions were made by the Rochdale pioneers in respect of :  
(a) members' voting, (b) distribution of profits, (c) meetings of members, (d) balance sheets, (e) cash trading ?
4. Explain the function of the Co-operative Wholesale Society.
5. What services are rendered to retail societies by the Co-operative Wholesale Societies ?
6. In what manner do the members of a co-operative store participate in the profits earned by the Wholesale Society ?
7. Write a short account of the organisation and administration of a retail distributive co-operative society.
8. Trace the evolution of the Co-operative movement in England.
9. Give an account of the modern growth and distribution over Great Britain of the membership of the retail distributive societies, so as to bring out the factors governing the increase of membership.
10. Can co-operation offer a solution to the problem of the equitable distribution of wealth ?
11. Describe the ideal of co-operative industrial organisation according to :  
(a) the producers' theory and (b) the consumers' theory. What difficulties have been encountered in applying these theories to practice ?
12. How do you distinguish between co-operative and capitalistic business ? Has co-operation any capitalistic features ?
13. What peculiar advantages are claimed for distributive co-operation ?
14. What, in your opinion, is the significance of the Co-operative movement in the industrial system ?
15. What procedure must be adopted for the registration of an Industrial and Provident Society ? In what principal respects does such a society differ from a joint stock company ?
16. "The apathy of the rank and file of co-operative societies to-day is the greatest hindrance to the development of co-operation." Discuss this statement, indicating the methods you would employ to secure a greater intelligent interest on the part of the members in their societies and in the wider development of co-operation.



## CHAPTER XXX

### MARKETING

As a business concept the term "market" is susceptible of various interpretations. Conceived in its widest terms, we understand by a market, not any particular market place in which things are bought and sold, but the whole of any region in which buyers and sellers are in such free intercourse with one another that the prices of the same goods tend to equality easily and quickly. The marketing process is that phase of business activity through which human wants are satisfied by the transfer of goods, services, and rights. It is the means whereby the producer or seller disposes of his surplus, and the consumer or buyer supplies his deficiency.

**SCOPE OF MARKETING.**—There is a common but fallacious theory that marketing is concerned chiefly, if not wholly, with finished goods, and is the activity of a specialised class of middlemen, or that it is limited to adding time, place, and possession utilities to completed material goods. The marketing process is infinitely more far-reaching than the transfer of goods from manufacturers to final consumers. Even considered only in terms of material things, it begins much earlier, as early indeed as the first movement of raw materials. Iron ore is marketed to the smelter, billets of pig iron in turn to the foundry; the foundry's product of castings to the motor manufacturer, who in turn sells cars to dealers from whom consumers buy.

If this comprehensive view of marketing be accepted, it is possible to apply it to a number of different spheres of activity. Amongst the various types of marketing systems, the following are the most important—

(1) **Marketing of Commodities.** Under this heading we may study the various systems for the distribution of raw materials, semi-manufactured goods, capital equipment, and consumers' goods. Any of these classes of goods may be marketed either from the producer directly to the consumer or to the manufacturer for further production; through organised commodity exchanges; through auctions; through co-operative organisations; or from the producer



through trading intermediaries, such as wholesalers, retailers, commission agents, and brokers.

(2) **Marketing of Services.** Under this heading we may study the numerous institutions engaged in providing and marketing a wide range of intangible services, such as transport, communications, news, insurance, or cleaning. Certain of these services are provided by private enterprise, whilst others may be provided by the State, as is the case with the Post Office in Great Britain, or the railways in many countries. The practice followed in marketing a number of these services is highly specialised, though the general principles of marketing applicable to tangible products may often be followed with advantage. The recent developments in the "selling" of railway service in this country indicate a new outlook on the marketing of services.

(3) **Marketing of Labour.** Strictly speaking, this is a subdivision of the marketing of services, but its importance is such as to warrant special consideration. Attempts to organise the local demand and supply of labour took place at a relatively late period in contrast to the creation of markets for other goods. Even now, the greater part of labour is marketed directly, through the labourer applying for a job, and by the prospective employer inserting advertisements in newspapers and posting notices at factory gates. Employment exchanges, some privately operated for a fee, others operated by the State at no direct cost to the labourer, now provide valuable assistance in helping the unemployed to find a job, and in providing the employer with a means of locating desirable and qualified workers.

(4) **Marketing of Capital.** The institutions engaged in this work constitute one of the most highly organised marketing systems in the world. The capital market comprises two sections: that dealing with short-term capital, and that dealing with long-term or investment capital. The first of these sections includes the joint-stock banks, the discount and acceptance houses, and the bill-broking firms, and is engaged in the finance of current industrial and commercial operations by the provision of working capital. The long-term capital market comprises issuing houses, investment trusts, company promoters, supplemented by the stock exchanges which provide a market for issued securities. Through these various agencies the savings and surplus funds of the community are



concentrated and lent to traders and others who require to borrow funds with which to carry on their business.

**REQUISITES FOR A DEVELOPED MARKETING SYSTEM.**—Exchange of goods occurs in the most primitive of societies, and trade between nations has flourished throughout history, but under modern capitalism marketing has become the central feature of the whole economic system. For marketing to attain this position, certain institutions are pre-requisite. The most important are private property—both in goods and in one's own person—freedom of contract and diffusion of property rights. If property rights are highly concentrated there will be little occasion for exchange through marketing; in a slave or strictly communal society, the advantages of specialisation would be achieved by some other means.

Given these basic institutions, certain devices are necessary to carry on the specific economic activities which constitute marketing. First, there must be devices for accomplishing transfer of ownership. In a developed form, this implies a vast system of law and recording. Equally fundamental are mechanisms for price determination. Prices can be determined by the higgling of individual buyers and sellers, but this process is usually least costly when aided by such facilities as those provided by commodity exchanges. The price mechanism is itself dependent on the existence of a unit of valuation, making possible a rational appraisal of various costs and their comparison with anticipated selling prices. Yet another essential to the organisation of specialisation by marketing is widespread information concerning the activities of specialists, and concerning the existence of supplies, desires, methods of transport, and localities in which trading can be done to advantage. Agencies for fixing standards of quality and for grading represent subsidiary aspects of the information function in the modern marketing system.

**MARKETING FUNCTIONS.**—Broadly speaking, the marketing process may be said to comprise two major activities—the concentration of economic goods, and their distribution or dispersion to the final consumer. Many raw materials, notably agricultural products, are produced at a large number of relatively small sources of supply, and need to be brought together in centralised markets in order that the various marketing processes may be performed efficiently. These concentrated supplies are then dispersed through the various



channels of trade to the ultimate consumers who require them. In the performance of this work, some or all of the following services may be performed—

(1) **Assembling.** This function may become necessary when the producers of a commodity operate only on a small scale, and are scattered over a fairly wide area. In such circumstances it may be necessary to concentrate supplies in bulk before proceeding with other marketing services in order to secure economy in handling. This is often found to be the case in the marketing of agricultural products. The same function may be performed in the case of manufactured goods where a dealer assembles a group of different commodities of a similar class for the convenience of his customers. The wholesale grocer, for example, may assemble in his warehouse a wide range of commodities obtained from different manufacturers in order to meet the requirements of retailers. This work of assembly may present special difficulties and call for exceptional skill in the following cases—

(a) Where the producers or manufacturers are numerous, small, and scattered.

(b) Where the commodity is little standardised, and is subject to considerable variations in quality.

(c) Where supplies are seasonal or irregular in character, thereby causing difficulty in the maintenance of stocks.

(2) **Grading and Standardising.** This marketing service is mainly of importance in connection with agricultural products, since manufactured goods are standardised in the process of production. The service of sorting out products into groups of uniform kind, quality, and size is known as grading. Standardisation aims at making it possible to give permanence to grades over long periods of time. The effect is to give confidence to buyers and to consumers generally, to lessen the volume of waste, and in general to pay the producer according to the quality of his produce, as well as to increase the demand by lowering his costs and by encouragement of the consumer through the sale of a definite article. Standardisation means, in effect, a widening of the market. Without a description that conveys the same concept of a product to both buyer and seller, it would be impossible to make a deal unless the goods themselves were at hand and inspected. If it were always necessary to examine produce before making a sale, it would be impossible to



deal in futures. In order to buy goods to be delivered at some future date, it is necessary to have some means of stating clearly what is being bought; and for products which are capable of being graded, the grade is the means of making such a statement.

(3) **Packing.** This function is frequently associated with manufacture rather than with marketing, but this is by no means invariably the case. Large national wholesalers, for example, not only grade and sort the merchandise in which they deal, but very frequently repack it under their own brands. Even small wholesalers have to unpack and repack most of the goods they handle. Not the least expensive part of the average wholesale business is the "broken package room," where orders from retailers, in quantities smaller than the manufacturer is prepared to pack separately, are made up. Packaging alone makes possible the branding and advertising of products, such as tea, coffee, rice, etc. If such articles are sold loose, only the word of the retailer exists to guarantee the brand, quality, and price. Packaging has given such goods individuality, since the manufacturer can advertise them and the public can identify them. In this way packaging has opened up new avenues of sale, and has enabled manufacturers to create demand in advance. With regard to agricultural produce, packing is of particular importance, especially as regards goods which are easily damaged, such as fruit or eggs.

(4) **Processing.** This function may be regarded as a manufacturing activity, since its primary purpose is to give a *form utility* to a commodity. Yet, inasmuch as it is often performed by a distributor, some mention of it is required. In the first place it may include conversion services performed on agricultural products, such as cheese-making, preserving fruit, or curing bacon. It may also take the form of a reduction of the bulk of commodities in order to make them more readily transportable, or the working-up of by-products. In certain food trades there exist certain specialised types of wholesalers whose principal function consists in buying different grades and qualities, and blending them in proportions which will provide an article acceptable to the consumer. Thus, there is the butter blender, the well-known tea blenders of Mincing Lane, while similar specialists exist in the coffee and other trades. Again, repairs and alterations undertaken as a subsidiary process in order to make goods saleable are obviously to be classed under the heading of



distribution rather than production. This is true of the alterations department of an outfitter who sells clothes ready-made, but is prepared to make slight alterations to make them fit the purchaser.

(5) **Market Research.** The object of market research is to secure information to aid in formulating and carrying out selling policies. It is concerned with a product in its relation to consumers, and covers not only the qualities of the product and the way it is packed, but the prices at which it is sold and the ways by which it is distributed to the public. There are various ways in which such investigations and experiments may be conducted. Trained investigators may be sent out to interview wholesalers and retailers or members of the public in their own homes, or questionnaires may be sent out through the post. Manufacturers may set up "laboratory shops," and use them as a means of collecting information about the demand for their own and their competitors' goods. New lines may be launched under controlled conditions or in sample areas, and the resulting sales analysed before an attempt is made on the market as a whole. The manufacturer or distributor who makes a wise use of these methods is likely to secure enormous economies in distribution, and escape a great deal of avoidable waste.

(6) **Salesmanship.** The chief objective of this stage of the marketing process is to bring a potential buyer into contact with a seller in such a way as to effect a transfer of goods. Salesmanship has been defined in a variety of ways by different writers. It has been said, for example, that "Salesmanship is the ability to persuade people to want what they already need," or that it is "the art of satisfying the need of the customer with goods and services, thereby establishing continuous and profitable relations between buyer and seller." The true salesman serves both his customer and his employer. He serves his customer by aiding him in the wise choice of goods which will best meet his requirements; he serves his employer by helping him loyally in the task of marketing his product without damaging the employer's reputation. As a result of this process there has been created what is termed "personal utility," which arises from the fact that economic goods are in the possession of a person who wants to consume them. If it were not for the activity of the seller in bringing to the attention of the buyer knowledge of new products that will meet his needs, the consumer might go



on for an indefinite length of time in ignorance of the existence of such goods.

(7) **Advertising.** Complementary to the foregoing function is that of advertising, which is an indispensable feature of modern marketing. The purpose of advertising is to sell, or to help to sell, goods, ideas, or services. Making a sale may involve many factors: arousing desire or creating demand; finding a buyer; negotiation of terms; giving advice or information, so that the buyer can use the product satisfactorily; and transfer of title. Underlying the problems of both salesmanship and advertising, we have the psychology of the consumer, but whereas the salesman considers each customer as an individual problem, the advertising consultant must consider them as a group and make his appeal accordingly. Advertising, in a general way, may be said to perform a two-fold function, viz. that of retaining the goodwill of existing customers, and that of securing the patronage of new ones. Advertising may be undertaken—

(a) To increase the sale of a given product or class of products without regard to individual producers. This can be done by co-operative advertising. E.g. the “Eat more fruit” and “Drink more milk” campaigns.

(b) To promote the sale of the goods of an individual seller by diverting trade from competitors.

(c) To inform the public of the production of an entirely new article which involves the creation of a new demand.

(8) **Transport.** Transport is the physical means whereby goods are moved from the point of production to the place where they are required for consumption, and, under modern conditions of specialisation, this function lies at the root of the whole marketing process. Heavy expenditure on transport is a necessary consequence of specialised and large-scale production, and is peculiarly characteristic of modern industry. There can be no real market, other than that of a local nature, unless goods can be moved safely, quickly, and at a cost which is not prohibitive. Under present conditions, the carriage of finished goods is performed partly by specialised agencies, such as railways, steamship, and other transport undertakings, and partly by manufacturers and traders who organise their own road transport departments.

(9) **Storage.** Goods are transported from producing points to



consuming markets, but after reaching the consuming market it is often necessary that they be stored until needed by the consumers. This function of holding the goods from the time they are produced until they are needed for consumption—the creation of time utilities—is just as necessary for the satisfaction of human wants as was the original production of goods. The existence of storage facilities enables producers and distributors to hold stocks at points convenient for regional distribution. Such stocks enable the seller to make quicker deliveries to buyers at distant points than if goods had to be shipped from the main plant. The buyers can carry smaller stocks and utilise their capital to better advantage. This aspect is particularly important in view of the modern tendency towards small-scale buying on the part of retailers. Storage is sometimes a service which is performed by special companies, though this is more often true in the case of raw materials at the port of landing and elsewhere than of finished commodities. A limited amount of storage must inevitably be undertaken by manufacturers, unless they make solely to order; and by retailers, unless they are merely acting as manufacturers' agents and conduct their business entirely by pattern or specification.

(10) **Finance.** Modern methods of production and marketing necessitate a considerable delay from the beginning of the production process until the finished product reaches the user. Generally speaking, the consumer, from whom the payment for the product is received, will not advance the money for the payment for the article until it is delivered. Provision for supplying the funds necessary must be made. The service of providing the credit and money needed to meet the costs of getting merchandise into the hands of the final user is commonly referred to as the finance function in marketing. The more familiar sources of finance are the commercial banks, commercial paper houses, and finance companies, which are all concerned mainly with the provision of short-term capital. The financial service may be given to the producer, to the merchant, or to the buyer. When we consider the case of the marketing of goods in the import and export trade, the finance function becomes both important and complex, since the geographical distance between buyer and seller, different national currencies, and the need for granting extended credit, impose special difficulties.

(11) **Insurance.** The ownership of property carries with it certain



risks, and since marketing has to do with the transfer of ownership, it is obvious that risk and risk-bearing are involved. The goods may be destroyed by fire, stolen by burglars, damaged by floods, losses may result from a fall in market prices, the goods may be rendered unsaleable by a change in demand perhaps resulting from a change in style or improved designs being placed on the market, goods may be sold on credit and bad debts incurred, or competition may render it impossible to sell goods at a profit. Many of these risks may be taken over by professional speculators, whilst others are assumed by the trader himself. In a period of great uncertainty, due to such a factor as currency instability, a trader in, for instance, dress materials, may safeguard himself against violent fluctuations by effecting a transaction in raw wool or raw cotton futures to offset his purchases of finished goods. More commonly, however, he himself shoulders the risk of changes in the value of his stocks after he has purchased them, and protects himself as best he can when prices are on the down grade by reducing his holdings to a minimum at such times. Apart from this, there are various possible ways of controlling marketing risks. Certain risks may be eliminated, some may be transferred, while others may be mitigated by different means. The development of cold storage, for instance, has practically eliminated the risk of spoilage of many perishables. Again, insurance companies, for a fee, assume certain types of risk under definitely specified conditions.

**TYPES OF COMMODITY MARKETING.**—When we consider the question of the marketing of material commodities, we are faced by a series of problems which are by no means uniform in their application. The commodities which flow through the channels of trade are of a diversity of types and are destined for a variety of uses. Some come from widely dispersed sources of supply, whilst others are produced on almost monopolistic terms; some are marketed to consumers all over the world, whilst others are required by a very limited number of buyers. Each commodity, therefore, tends to have its own characteristic mode of distribution in the light of these relevant facts, but for the purposes of generalisation we may reduce them to a number of classes, of which the following are examples—

(1) **Primary Products.** These include the products of the extractive industries, such as agricultural produce, minerals, forest products, and fish. The distinguishing feature of the members of this group



is that they are taken directly from nature and turned into the channels of industry. Moreover, in the great majority of cases some preliminary work on them is necessary before they are available to the consumer. Many of these commodities are dealt with on the *produce exchanges* which include some of the most important markets in the world. Each is characterised by being centralised in some important city, though embracing practically the whole world in the scope of its operations. For instance, the Corn Exchange in Mark Lane is devoted to the sale of all sorts of cereals and agricultural seeds; tea, coffee, cocoa, and rubber are disposed of principally at the Commercial Sale Rooms in Mincing Lane; wool is sold at the Exchange in Coleman Street, London, and also at Liverpool and Bradford; whilst fruit and vegetables find their chief sale at Covent Garden. *Auction sales*, again, are of considerable importance in the wholesale trade in certain commodities, such as fruit, wool, and furs. In some cases, the marketing problems in connection with these commodities are simplified by reason of the fact that industrial or distributing firms handling them acquire control of sources of supply. Again, dealings in these materials are often the subject of cartel agreements which may be international in scope.

(2) **Semi-manufactured Products and Manufactured Parts.** These possess the common characteristic that although certain industrial operations have been performed upon them, they are not yet available for the final consumer. Manufactured parts are articles which are incorporated, without modification, with other materials or parts in the completed products. These range from the pressed metal parts used in the manufacture of electrical meters and calculating machines, to glass insulators and containers, motors for vacuum cleaners, and motor-car bodies. The market for these parts is essentially a *vertical market*, that is, a market by industries rather than by functions extending through diverse industries. In the case of a manufactured part like a motor-car body, the market is found only in a single industry. A company manufacturing pressed metal parts on the other hand, finds its market in a series of industries, but the purchases in all cases are made with reference to a single industry. Semi-manufactured products also become part of other manufactured articles, but undergo physical modification in the further processes of manufacture. Examples of these are steel plates



and rods, copper wire, leather, and book paper. The market for these materials is again usually a vertical market by industries. Some such materials find use in various industries as, for example, copper wire, but for many materials the market is confined to a single industry, as in the case of wool tops.

(3) **Manufactured Consumers' Goods.** Under this heading we may include the great bulk of the goods which are purchased by the final consumer. They comprise the necessities, comforts, and luxuries of life for which the consumer pays approximately £1,750,000,000 per annum in this country. The goods purchased by the final consumer are mainly marketed through some form of retail concern, but the channels whereby they reach the retailer are both numerous and complex. The small-scale demand of the individual consumer necessitates convenience and accessibility in the location of the store, and a variety of grades, styles, sizes, designs, prices, and other qualities. Furthermore, a number of services, such as credit, delivery, demonstrations, repairs, and many others which the manufacturer cannot economically give, are expected by the consumer. Hence a large number of retail outlets exists for disposing of these consumers' goods, including the independent retailer, multiple shops, departmental stores, mail order houses, and co-operative retail societies. Again, a considerable volume of produce, mainly of a perishable type, is distributed to the consumer by itinerant traders.

(4) **Capital Equipment.** This includes manufactured goods bought by producers, merchants, and institutions, not for resale, but for the purpose either of aiding in the production of their product, e.g. factory and office equipment, or of adding to their equipment or maintaining it. The selection of such equipment is governed by the product which is to be turned out by the plant, or by the nature and scope of the operations to be performed. The market for installation is one in which repeat demands are infrequent. Its purchase requires capital expenditure, and is governed in large measure by general conditions in the particular industry in which the equipment is to be used. In the sale of complete plant installations, engineering and designing service is of importance. The market for capital goods of this type is extremely specialised, and is usually limited to one industry. Accessory equipment is the auxiliary or supplementary equipment of a plant; it serves to



facilitate the operation of the main installation, to aid in carrying on administrative and auxiliary services, and to assist in the performance of other miscellaneous tasks. Examples of accessory equipment are small motors, tools, time clocks, conveyors, factory trucks, and steel shelving. The market for an item of accessory equipment cuts across many industries. In approaching this market, therefore, it is necessary for a manufacturer of accessory equipment to ascertain the types and sizes of firms which are potential purchasers, and to exclude from his sales programme those firms which are too small to use the products which the company produces.

### TEST PAPER XXX

1. What is a "market"? What conditions are necessary in order to ensure a wide market for a commodity or service? Name some of the chief markets, and state the purpose for which they are used.

2. Enumerate some of the marketing problems which arise from the separation of the producer from the consumer.

3. Name four important functions of marketing, and state the causes which give rise to the need for each of them.

4. Show how the assembling of goods is affected by the scale of production, and the extent of division of labour.

5. Mention as many factors as you can think of which must be kept in mind in choosing a package for use in distributing a product through the retail trade.

6. What part is played by (a) market research, (b) salesmanship, (c) advertising, in the marketing of goods?

7. What is the use of storage? Draw up two curves, one showing your idea of the probable fluctuations of the price of eggs during the year if there were no storage facilities; the other showing the probable fluctuation with storage.

8. Certain areas in London are world-famed as markets for specific products. Name the principal markets and describe, in some detail, the activities of one of them.

9. Analyse the influence which developments in the grading of a product have upon the organisation of the market for that product.

10. Discuss "grading" as an aid to the marketing of products, and give illustrations of recent practice in this direction.

11. Outline the principal marketing functions which may be performed by training intermediaries in the distribution of goods from producer to consumer.

12. "Marketing does not really help. Indeed it hinders. Time and energy are spent in merely passing goods on." Comment on the correctness or incorrectness of this statement.



## CHAPTER XXXI

### THE MIDDLEMAN AND HIS FUNCTIONS

It has been seen in an earlier chapter that there are three main groups of persons who enter into consideration when dealing with trade : the producer, the trader, and the consumer. The trader's function, which was formerly exercised by a single person, is to effect the exchange of the goods by purchase and sale ; and, under normal circumstances, this is now subdivided into three divisions : the *collecting*, the *distributing*, and the *intermediary* trader. As the growth in the variety and complexity of trading operations necessitates a more extensive division of labour, this is expressed in the increase of members in each of the three main groups. In actual practice, it often happens that goods in their distribution from the producer to the consumer change hands five, ten, or even more times, in such a manner that (just as fire buckets and bricks are passed from one person to another) the individual members concerned work hand in hand.

In addition to the various intermediaries which assist in the transference of goods from place to place, there is a large number of necessary and allied activities, such as the methods of payment and financial facilities, warehousing and insurance, the supply of information concerning the standing of clients, etc. In this way, there is brought into existence an extensive division of labour for effecting the exchange of the goods, so that the trade organisation may be compared with the links of a chain, since the function of one individual forms a connecting link with the others.

**FUNCTIONS OF THE MIDDLEMAN.**—The term “middleman” in its widest connotation embraces all those who intervene between the primary producer and the ultimate consumer in the exchange of commodities. It is sometimes confined, however, to the mediating links which are inserted between the wholesale and the retail trade which we have already described as *intermediary* traders. They include dealers, wholesale merchants, manufacturers' agents, factors, and similar undertakings which sandwich themselves in



between the wholesale and retail trade, or between the manufacturer and the wholesaler. In addition to the ordinary functions of buying and selling, the middleman may perform some or all of the marketing functions explained in Chapter XXX. Thus, it is the function of the middleman, working in the producing area, to buy up supplies from scattered producers and concentrate them at certain points before distribution in the area of consumption can be economically carried out. The middleman must, in his own interest, divert the goods to the most favourable market for them. An irregular flow of goods to market causes wide price fluctuations, resulting in losses to dealers and having an undesirable effect on buyers.

The middleman can also utilise existing transport facilities to the best advantage by forwarding in bulk in order to take full advantage of special freight rates and other concessions. Goods are transported from producing points to consuming markets, but after reaching the market it is often necessary that they should be stored until needed by the consumers. Storage has always been recognised as a fundamental economic service in the smoothing out of supplies. Moreover, it is not always possible for the producer of goods to wait for his money until the consumer pays for them. Frequently this function of waiting is performed by the middleman, who takes the goods from the producer and pays for them within a short period, retaining possession of them until he can dispose of them. Even after disposal he may still finance the goods through extended credit. He may also render such specialised services as grading, packing, and processing.

**Example of a Middleman.** A good example of a middleman engaged in the home trade is the *coal factor*. A colliery company frequently sells its coal direct to a factor who disposes of his supplies to smaller dealers and distributors. The business of the colliery company is to get coal to the surface. The business of removing that coal from the pit-head and financing it until it can be delivered to a consumer is quite a different function from that of coal-mining. It can be performed by the colliery company itself. It sometimes is, but when it is so performed the company requires additional capital for the conduct of that side of the business, which capital requires remuneration commensurate with the risk involved. The factor performs a function exceedingly useful, and indeed vital to the coal industry,



but imperfectly understood by the general public. It is he who facilitates the business of those smaller merchants who do not attend the Coal Exchange. In many cases he actually finances the coal from the time that it is brought to the pit-head until the time that these smaller merchants can take delivery of and distribute it. It is necessary for the conduct of the trade that a certain supply of coal should always be available to meet current demands or an unforeseen emergency. This means that somebody, in practice the factor, must purchase a quantity of coal and, in addition to taking the risk of the price at which he may be able to dispose of it, must hold it for a period running from days to weeks, during which period he will receive no interest on the capital he has sunk in the purchase of the coal.

In many cases the factor provides the wagons in which the coal is removed from the colliery. In other cases he steps in to remove congestion, either at the pit-head or in the railway sidings, by purchasing a number of wagon loads of coal at a time when the market is very slack, and, by his knowledge of the markets all over the country, distributing the coal wagon by wagon, and thus enabling the collieries to continue production. For that service to the colliery company he doubtless receives, and is entitled to, a concession in the price that he pays for the coal.

Besides giving his buyers the benefit of his intimate knowledge and experience of the particular coalfield, the factor may also undertake the grading and cleaning of coal, both for household and industrial purposes. Thus he ensures only those coals being supplied which will meet the special requirements of his customers.

**INCREASE AND DECREASE OF MIDDLEMEN.**—In the organisation of trade, two striking tendencies are noticeable—

(1) The tendency for a larger and larger number of middlemen to assist in the conduct of trade (i.e. division of labour).

(2) The opposing tendency to eliminate existing middlemen.

These two tendencies can best be seen in the sphere of *manufacture*. In the Lancashire cotton industry, one firm spins yarn ; another buys and weaves it ; and the goods are dyed, bleached, or finished by a third firm ; and marketed by a fourth. On the other hand, the large woollen manufacturing firms sort, dye, and prepare their own wool or other raw material ; spin, weave, mill, dye, finish, and market their own goods. The question arises as



to which is the better system of the two : that which prevails in the cotton trade and, to some extent, in the worsted trade ; or that which prevails in the woollen industry ? Some say one system and some the other. Among the advantages of the combined system there is—

(1) Greater unity of purpose (e.g. the wool buyer has in his mind not merely the making of a yarn to sell, but the production of the best result in the finished cloth).

(2) There are various economies of service : the cost of extra books, and buying and selling apparatus between one department and another, is saved.

(3) A business organised on a large scale can afford to buy large and expensive machines.

(4) Greater expedition in quickly executing large orders for large customers.

(5) The system enables the departmental managers to specialise more highly each in his own department.

Against these advantages there are certain inevitable disadvantages—

(1) The absence of a check upon the cost of work in any particular department which the putting out of work secures.

(2) The difficulty of securing efficient central management. Without this essential, a large business becomes unwieldy and less efficient.

Both these tendencies, although opposed to each other, are based upon the same principle. It is the striving after greater economy with the object of a greater return to capital.

These same conditions also exist in *trade*. Every trader who desires to establish a business has two ways open to him—

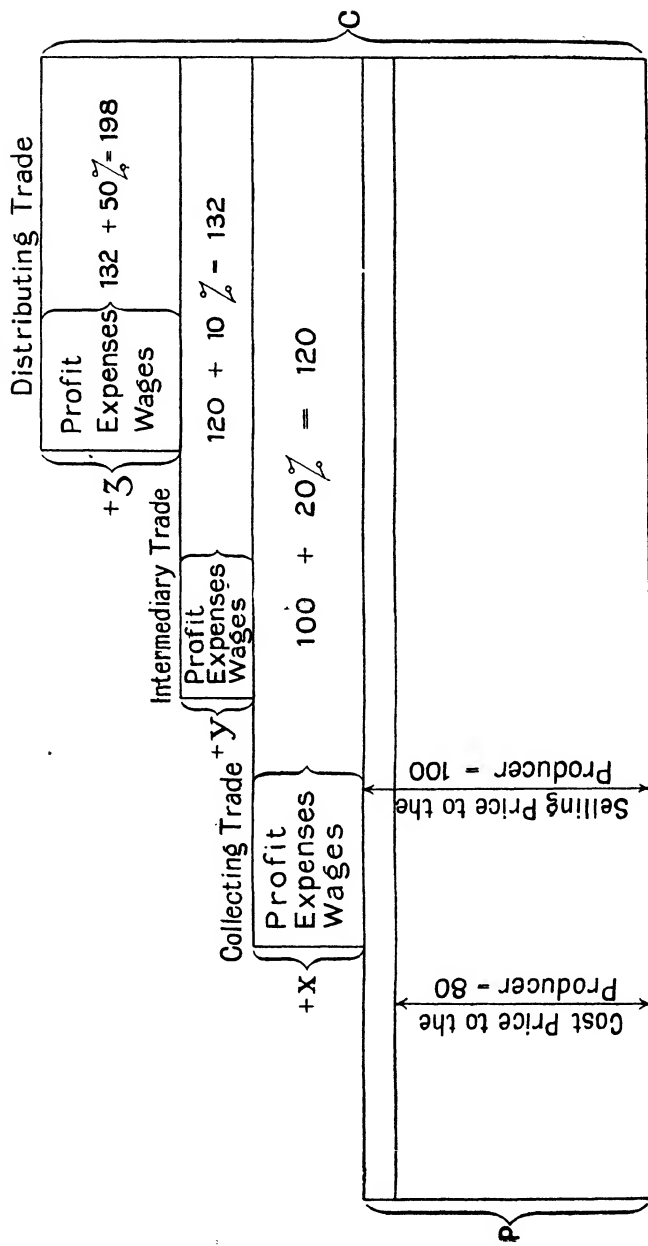
(1) He can set up his new undertaking alongside others of the same kind, thus entering into competition with them ; or

(2) He can endeavour to enter as a useful and indispensable link in the existing chain of organisation.

If he chooses the former method, his business prosperity will depend upon whether he is triumphant in the competitive struggle, and this can be attained only by effecting a cheaper and more economic exchange of goods than his competitors. He must, therefore, ever be on the alert to discover the best and cheapest sources of supply, so that he can effect his sales in the best market.



# THE ELEMENTS WHICH CONSTITUTE PRICE





In this endeavour he is often led to skip over certain members in the trade organisation wherever such a course of action offers an advantage.

The tendency to exclude certain links in the chain of exchange usually arises from the action of traders themselves, but it may also take place owing to the action of producers and consumers. This latter phenomenon will now be examined.

**EFFECT OF MIDDLEMEN ON SELLING PRICE.**—As already explained, each new link in the chain of trade organisation creates a new set of opposing interests, since there is involved an additional sale and purchase, for the goods have to pass through the hands of another middleman. Naturally, each additional member increases the selling price, and each increase is usually made up of the total of his expenses (i.e., the remuneration of his labour) and the profit as a return for his risk. The consequence of this is that each new opposing interest must also increase the price of the goods, as is seen in the diagram on page 361.

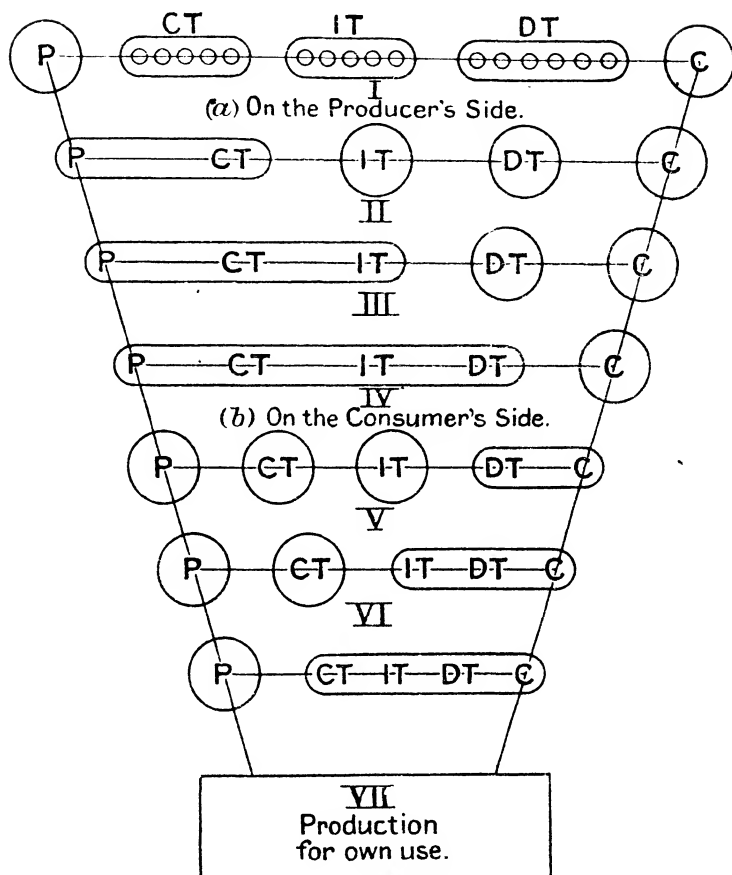
The expenses of the process of distribution fall ultimately upon the producer and consumer, both of which benefit by any progress in trade organisation, in the mode of transport, or in the diminution in the number of middlemen. Thus, any increase in the expenses of distribution caused by the increase in the number of middlemen falls as a burden upon the producer and the consumer.

In many directions there is a tendency at the present time to eliminate rather than to engage a larger number of middlemen. Farmers, manufacturers, and even retailers, organise themselves, in many cases, for the purchase, in common, of raw materials, machinery, seeds, manure, etc. The tendency is for them to trade direct with the wholesale dealer. On the other hand, the consumers organise themselves in co-operative societies, with the object of personally effecting their own purchases. Their aim is to exclude the retail dealer. Further, on the great centralised produce exchanges, rings and other powerful groups of speculators are formed, whose endeavour is to monopolise the world market in some particular commodity, such as cotton, copper, wheat, silver, etc. In this way, they hope to weed out those persons who have previously carried on business in that particular branch of trade.

**METHODS OF ELIMINATION.**—The various methods of elimination are best illustrated by the diagram on page 363.



## METHODS OF ELIMINATING MIDDLEMEN



- I. Producer combines Sale of Goods and function of Collecting Trade.
- II. Producer deals directly with Distributing Trader and thus eliminates, Collecting and Intermediary Traders.
- III. Producer establishes Stores or branches, and serves direct (e.g. typewriters, shoes, etc.).
- IV. Consumer eliminates Retailer and buys direct from Wholesaler.
- V. Consumer buys directly from Collecting Trader, and thus eliminates Distributing and Intermediary Traders.
- VI. Consumer buys directly from Producers (e.g., Mail-Order Business and Co-operative Society).
- VII. Consumer links Co-operative Consumption with Production.



Stages I, II, and III represent the efforts made by the producers to eliminate certain of the middlemen. In the *first stage*, the collecting trade is omitted, so that the distribution is effected direct with the intermediary trader.

In the *second stage*, the intermediary trader is omitted as well as the collecting trade, so that direct relations are entered into with the retailer. In this way, manufacturers seek to deal direct with the retail trade.

In the *third stage*, the manufacturer opens shops for sale direct to the consumers. The whole of the trading operations are thus linked on to the production, and the independent traders become dependent organs in the service of the manufacturer or other producer.

The stages marked IV–VII show the attempts to eliminate on the part of the consumers.

*Stage IV* illustrates the omission of the distributive trade by the establishment of co-operative societies.

*Stage V* shows the exclusion of the intermediary trade by direct intercourse with the collecting trader, as in the case of State undertakings.

The last and *highest stage* consists in the complete elimination by the consumers of all opposing interests, so that the societies of consumers absorb the process of production, and have, as their aim, production for their own needs. The beginnings of such a system are to be seen in the establishment of the large factories and workshops in connection with the English Co-operative Wholesale Society.

Recent changes in the distribution of the population of Great Britain emphasise the importance of the services of the middleman. They undoubtedly constitute an essential part of the total cost of production. The people who perform these services may be supplanted by other individuals or groups, but the services themselves must be continued. We may speak of eliminating the middleman, but we cannot dispense with the services he performs. They are a vital part of the mechanism of production. But we may reasonably ask whether these services are being conducted in the most efficient manner. The system of private enterprise must stand the test of efficiency and the community has a right to object if any set of producers or traders is not efficient.



## TEST PAPER XXXI

1. In what respect may the organisation of trade be compared with the links of a chain?

2. The middleman has been the target of the most vicious attacks. It has been charged that he collects a profit from the distribution of goods without rendering any service for it.

(a) Do you agree with this charge?

(b) If not, enumerate the services which he does perform.

3. How far do middlemen co-operate to assist in the preparation of goods for sale (i.e. in sorting, grading, blending, etc.)? Explain by one or two commodities with which you are familiar.

4. Explain in detail the services performed by a typical middleman engaged in some branch of the home trade.

5. Mention the advantages and disadvantages of conducting a variety of manufacturing processes under one management.

6. Enumerate the advantages to be gained from specialisation. Illustrate your answer by reference to the organisation of the Lancashire Cotton Industry.

7. Trace the effect of the increase in the number of middlemen on the Selling Price.

8. Give illustrations of some of the methods by which middlemen are eliminated.

9. Give two concrete cases to show that both "producers" and "consumers" are instrumental in squeezing out the middleman.

10. Outline the chief reasons for the decline in importance of the middleman in certain trades, and for his increasing importance in others.\*

11. Do you think it desirable and possible to do away with the middleman?

12. Describe carefully the services rendered by the wholesaler to the retailer. Name instances in which the wholesaler is omitted in the passage of goods to the retailer from the manufacturer.

13. In what ways are "middlemen" useful to commerce? Illustrate by reference to some class of middlemen with which you are acquainted.

14. Give some examples of sale direct to consumers by manufacturers and discuss why this method of distribution is not adopted more generally.

15. Do you know of any instances in which the wholesaler is passed over in the passage of goods from manufacturer to retailer? What do you consider to be the reasons for the omission?

16. There is a pretty general hue and cry for the elimination of the middleman. Enumerate some of the functions performed by him which tend to justify his continued existence.

17. "It is the merchant rather than the maker who is the hub of the modern economic system with its dependence on the mechanism of price." Refute or justify this statement.

18. "We may speak of eliminating the middleman, but we cannot dispense with the services he performs." What are these services?

19. Indicate the services to the community performed by the dealer or middleman. Show how errors may arise concerning the nature and amount of his gains.



## CHAPTER XXXII

### THE RISKS OF TRADE AND THEIR DISTRIBUTION

THE solution to many of the problems connected with *direct* purchase and sale is based upon a proper understanding of the various kinds of risk and their distribution over the various members of the trade organisation. These risks are mainly connected with the following—

- |                      |   |
|----------------------|---|
| 1. Price             | 4. Delivery                               |
| 2. Credit            | 5. Quality                                |
| 3. Rates of Exchange | 6. Fluctuations in the<br>volume of Trade |

**PRICE RISKS.**—A glance at the movement of the market prices of various goods shows at once that prices are subject to great fluctuations.

In fact, within the whole sphere of trade, there are but few articles the price of which is not subject to great fluctuations. These fluctuations are the greater, the more these goods resemble raw materials; whereas the further the commodity progresses in the stages of manufacture and approaches its complete state, the smaller do the fluctuations become.

After a consideration of the immense stocks which must always be at the disposal of trade on the world's market (e.g. two years' supply in the case of wool and at least one year's supply of American cotton and Brazilian coffee), it can easily be seen that a 10 per cent. alteration in price changes enormously the total value of these available stocks.

As every trader who has accumulated a stock of goods for a shorter or longer period gains or loses with each fluctuation in price, it follows that a risk is thus involved.

Leaving out of consideration the quantity of stock concerned, this risk increases with the length of time between the purchase or manufacture of the goods and their sale or consumption, combined with the number of fluctuations in the particular commodity. Although many of these risks can be thrown on to other members of the trading organisation, the trader cannot avoid them entirely.



Again, if the risks are borne by a number of persons instead of by a single trader, it must be remembered that the risk is still in existence, although it is distributed in a different way. From this it will be seen that the greater the number of risk-bearing middlemen, the smaller does the price risk become in respect of each individual trader. Every additional member engaged in the work of distribution bears a part of the total risk, and this diminishes the amount borne by other members. On the other hand, if a middleman is eliminated from the trade organisation, the risks he has hitherto undertaken must be borne by the new member, who has assumed the execution of the work. Hence, the trader who buys and sells direct, without the aid of a middleman, undertakes a greater risk in connection with price fluctuations.

**CREDIT RISKS.**—Every independent trader through whose hands goods pass is, at one time, “buyer” and, at another, “seller.” If the transaction is not concluded immediately, there arise credit conditions, so that one person is the debtor, whilst the other is the creditor. For the trader granting the credit, a risk is involved, which increases with the length of time between the date of purchase and that of payment, and with the increase of distance between creditor and debtor. If business is transacted directly with customers without the intervention of intermediaries, the credit risks on the part of the direct seller will increase. If trade is effected direct, say, between manufacturer and consumer, the organisation for protecting credit is dispensed with. Thus, the experience of hitherto existing traders, and their system of organisation and specialised knowledge, as well as the service of inquiry, etc., are eliminated, so that the risks devolving upon the manufacturer or producer must necessarily increase.

**EXCHANGE RISKS.**—If both buyer and seller reside in different countries, each of which possesses its own system of currency, there arises the need for collecting the price of the goods at exchange rates. Since the adoption of gold as the world standard, however, the fluctuations in these rates (in normal times) have considerably diminished; although, even in countries with a gold standard, these fluctuations may still amount to 1 or 2 per cent.

In countries with a silver or paper standard, the circumstances are totally different, for here the fluctuations may become very great. It is evident that, with the elimination of the middlemen,



the risks caused by fluctuations in exchange rates are by no means abolished, but they are merely readjusted so that they devolve upon the person who takes over the work hitherto connected with that risk.

Hence, in the case of a more direct policy of purchase or of sale being adopted, the risks connected with the exchange rates, and formerly borne by middlemen whose services were involved, will now be undertaken by the person engaging in direct trade. From an economic point of view, it is immaterial which party bears this risk, although it may be that the eliminated middleman is able to exercise more skill in utilising the state of the exchanges than the member who takes his place, or vice versa.

**DELIVERY RISKS.**—The adherence to the date of delivery constitutes a very important factor in trade. If the goods ordered are not delivered at the proper time, an immense loss may ensue to the parties concerned. Every member in the trading organisation is in this respect dependent upon the preceding process of production, but is responsible to the succeeding member. Hence, between each person engaged in the distribution of goods, conflicts may arise which involve greater or smaller risks, in case there is a failure to adhere to the appointed period of delivery.

One of the important functions of a middleman is to attend to the fulfilment of contracts with regard to delivery, and especially in the case of goods for exportation. Where the services of a middleman have been used for this purpose, his elimination will mean the assumption of greater responsibility by the person who intends to trade more direct ; that is, the direct buyer or seller will have to undertake greater risks in connection with the delivery of the goods.

**QUALITY RISKS.**—The practical merchant is well acquainted with the numerous claims, deductions, lawsuits, etc., which arise out of complaints concerning the delivery of goods. In the same way, the trader who has to sell goods as they are received from the manufacturer or other creditor is well aware of his responsibility to deliver in conformity to sample or to quality previously agreed upon. The avoidance of disputes with his customers in this respect is often one of the most difficult duties of the trader, especially where unscrupulous persons are concerned. Such persons may even invent grounds for complaint in order that they can refuse



to honour the contract, whenever the market conditions change to their disadvantage.

Under these circumstances, one of the most important duties of the trader is the checking of the goods purchased and a still more careful checking of the goods dispatched, and for this work a thorough knowledge of the commodities themselves is indispensable. It is chiefly for this reason that it is difficult to eliminate a person from the trade organisation who has hitherto performed this work, and direct buying and selling encounters great difficulties in view of the existence of these quality risks.

On the other hand, there are some cases in which the trader, manufacturer, or consumer endeavours to organise the most direct purchase possible, so that the work of selection can be personally undertaken at the place of production, or because a greater influence may be exercised over the producers in causing them to deliver the goods in conformity with particular requirements. This is seen in such goods as watches, embroidery, and various kinds of machinery. Hence, the risks in connection with quality may operate not only as a hindrance to elimination, but also as a factor assisting it.

**MARKET RISKS.**—As far as the price is entailed, market risks have already been discussed; but there are other factors to be taken into consideration by the trader. In the first place, he must endeavour to analyse the various symptoms of the rise and fall in the market, and to modify his business accordingly; to provide himself with a stock in good time for a rise in the market price; and to abstain from buying during a period of depressed trade. These tendencies will be the more quickly and correctly grasped, the closer the trader keeps in touch with production and consumption, rather than being separated from them by various middlemen. Moreover, these indirect sources of information are often unreliable, and it should be the trader's aim to keep secret his knowledge of market forces and his arrangements in connection therewith. In this case, the most direct trading relations are preferable (i.e. direct purchase and sale).

There is another factor to be considered—the sudden rise or fall of the market. This operates the more slowly with the increase of middlemen in the process of distribution. Each member engaged in trade offers a certain amount of resistance to sudden alterations



in market conditions, since it is to his interest to maintain a steady course of business. Hence, middlemen help to stem any sudden changes from high to low prices and to increase the steadiness of the market. Whether this retarding influence on the market fluctuations is an advantage is very questionable.

Thus, the carrying on of any business is inevitably accompanied by risks; risks very numerous, of a diverse nature, and varying in importance. These risks may be guarded against in the vast majority of cases by insurance with a company which makes insurance its business. But insurance is expensive, and this factor of expense precludes the covering of all risks, otherwise it would only be necessary for every business to insure its profits. Since it is impossible to cover all risks on the grounds of expense, the best course is to cover those risks of loss which the business could not afford to meet, whilst not unduly diminishing profits by too heavy insurance premiums.

The study of the risks of trade and their distribution over the members engaged in trade has brought the student a step nearer the principal problem, viz. whether direct trade is to be preferred to indirect, and whether the increase or the diminution in the number of middlemen is desirable.

### TEST PAPER XXXII

1. Enumerate some of the chief risks in connection with trade.
2. "The trader who buys and sells direct, without the aid of a middleman, undertakes a greater risk in connection with price fluctuations." Explain and criticise this statement.
3. Explain how "Credit" risks arise.
4. Why do risks occur in connection with the payment of debts to traders resident in a foreign country?
5. Upon which members of the trading organisation do those risks fall which are connected with the delivery of the goods?
6. In what respect do middlemen help to increase the steadiness of the market?
7. The trader, it is said, has to carry certain risks. Explain the principal risks he has to carry, and the manner in which he is rewarded for carrying them.
8. The wholesaler is an intermediary between the manufacturer and the retailer. Describe the ways in which he renders services to them, and indicate any special business risks which he shoulders.



## CHAPTER XXXIII

### ORGANISATION OF THE IMPORT TRADE

THE significance of the import trade is due to the fact that the population of Great Britain is to a large and increasing extent dependent for its food and the materials of its industry on supplies from abroad. The average annual value of our net imports of food and raw materials amounts to nearly £800 millions. About four-fifths of our supply of wheat and flour and three-fifths of our supply of meat come from abroad. Coal is the only raw material in which Great Britain is self-supporting. The whole of the cotton, nine-tenths of the wool and timber, and more than a third of the iron ore which we use are imported from overseas. During the last century there has been a steady growth in our dependence on overseas supplies for the essential means of existence, and, in the studied opinion of the Balfour Committee on Industry and Trade, there is not the slightest reason to expect that the tendency will be arrested or reversed in the near future.

The possibility of producing in Great Britain a larger proportion of the essential raw materials of our industry is severely limited by climatic and geological conditions, and though, no doubt, new discoveries and methods of production may here and there enable a home product to be substituted for an import, the aggregate result of such changes cannot affect the broad outlines of the picture.

**GENERAL ORGANISATION OF IMPORT TRADE.**—The diagram here shown will serve to illustrate the general organisation of the import trade. In order that the student may obtain a firm grasp of the relationship existing between the producer and the consumer, all the main functions of trade have been included. Of course, all these functions will not come into play in every transaction, but there will be a variety of combinations according to circumstances.

An examination will first be made of those trading functions proper which are marked in Roman figures on the diagram, each of which appears as buyer and seller of the goods during their distribution to the consumer, and through whose hands the goods pass as property.

No. 1 represents the *supplier* of goods in the country of exporta-



tion, and No. IX the English *consumer*. Since they both play a passive part in the trade itself, they may be left out of consideration. Hence, in analysing the diagram, it only remains for the student to consider the seven traders proper (marked Nos. II to VIII). Nos. II and III are engaged in the *Collecting Trade*, whilst Nos. VII and VIII are concerned with the *Distributing Trade*. Nos. IV to VI represent the trade conducted by *Intermediaries* in the centralised market.

**COLLECTING TRADE.**—The first class of traders through whose hands the commodity usually passes on leaving the supplier or producer is that of the collecting trader. The main object of this branch of trade lies in the purchase of large or small quantities of goods, their receipt, supervision, assortment into various qualities, preparation for transport, and the transference of the goods to a larger warehouse to enable them to be handed over to the wholesale dealer. The functions of the collecting trade, like that of the distributing trade, are undertaken by two members—the small collector and the large collector. The first of these comes into direct communication with the primary producer, and must not only be able to judge the conditions of the market, but also possess a good knowledge of the goods themselves. He must be in constant touch with both small- and large-scale producers, and know their methods of trade, the extent of their output, their financial standing, as well as enjoy their confidence. Of course, this is possible only where the collecting trader acts in good faith and keeps to his word, carrying out punctually his promises and obligations in reference to acceptance of the goods, payment, etc. This first function of collecting, as shown on the diagram under No. II, may be effected by—

- (a) A private buyer working on his own account.
- (b) An agent, who is engaged in effecting the purchases for the wholesale firm ;
- (c) A large-scale producer, who combines the function of collecting with that of production ;
- (d) An association of producers, who form a selling association, or cartel, the latter undertaking the collection of goods from the producers.

Whichever of the above methods of collection be adopted, the buying area is naturally restricted to a definite locality.



A much larger purchasing area comes within the sphere of the wholesale collector, who is marked No. III on the diagram. To him the various small collecting traders deliver their products, or he may send his numerous agents into the purchasing area.

The wholesale collecting may be effected either by—

- (a) A dealer trading on his own account ;
- (b) A commission agent.

Both these traders may utilise the services of the warehouse, market, fair or exchange, prior to the disposal of the goods to the exporter.

**INTERMEDIARY TRADE.**—The members of the intermediary trade are marked on the diagram Nos. IV, V, and VI, and consist of—

- (a) The exporter in the country of origin, who draws his supplies from the wholesale collecting trade ;
- (b) The importer in England ;
- (c) The wholesale dealer engaged in the import trade.

These traders not only have extensive capital at their disposal, but have also far-reaching trading connections with all the important points of the world market. They engage in the import and export trade without being tied to fixed relationships. On the other hand, however, they so utilise market conditions, that they are able to bring their goods to certain central points, from which they can then easily be conveyed to the most favourable selling areas at home or abroad. The place of business of an intermediary may be anywhere, since, on account of the well organised system of communications and widespread means of warehousing, it is easy for him to dispose of his goods from any point. However, his head office is usually to be found in one of the great trading and warehousing centres of the world.

When the goods have been sold by the exporter in the country of origin to the English importer, there are three distinct classes of operations performed by the English intermediaries engaged upon the produce exchange—

- (1) The importation of consignments of goods by the import merchant ;
- (2) Sale by auction of the goods in lots by the brokers acting for the importer ;
- (3) Purchase by the wholesale dealer from the broker in large quantities.



It will be seen from the diagram that the last member of the intermediary trade, viz., the wholesale dealer engaged in the import trade, and marked No. VI, may dispose of his goods in a variety of ways—

(1) He may tranship a portion of his goods to foreign markets ;

(2) Another portion may be sold through his agents to home manufacturers, as in the case of such goods as raw cotton, tobacco, etc. ;

(3) Another portion may be sold to the wholesale dealer in the home market ; and

(4) He may supply the Co-operative Wholesale Society, which, in turn, will distribute the goods through the retail societies. These may further dispose of the goods to their own organised members, or to individual consumers who are non-members.

**DISTRIBUTING TRADE.**—The members of the distributing trade are marked Nos. VII and VIII on the diagram. In this class of traders is included, not only the retail dealer, but also the wholesale dealer engaged in the home market, whose object it is to supply the retail dealers within his selling area with the commodities they require. The wholesale dealer No. VII, who is engaged in the home market, has quite a different function to perform from the wholesale dealer No. VI. Whilst the latter is engaged as an intermediary in the world market, and occupies himself with the purchase and sale of a single commodity (such as coffee, corn, cotton, etc.), No. VII is a distributing trader engaged in the purchase and sale of a variety of different commodities. Again, wholesale dealer No. VI supplies a large area with a single article only, whilst No. VII supplies a smaller selling area with the various goods in his line of trade. Thus he may deal in coffee, tea, sugar, and provisions generally.

The last link in the distributive trade is occupied by the retail dealer No. VIII, to whom is allocated the task of holding an available stock of goods to meet the requirements and wishes of his customers, and to sell these goods in small quantities to the individual consumers.

From what has been already said, it will be seen that a commodity passing in the regular way through the hands of all the members engaged in the import trade (marked I to IX), changes



hands no fewer than eight times. It is eight times the subject of a purchase and sale, regardless of the possibility of its repeatedly becoming a factor on the speculative exchanges as either a floating or warehoused commodity. Since each trader adds to the price the threefold increase of trading expenses, wages, and profit, it is clear that the entire organisation diminishes the price of the goods to the producer and increases them to the consumer. It is, therefore, the aim not only of the producer and consumer, but of every middleman, to simplify the method of distribution by the elimination of all unnecessary members.

**THE IMPORTATION OF TEA.**—Supplies of tea reach this country from India, Ceylon, Java, Sumatra, and China. The northern Indian crop is far the heaviest of any country of production. The plucking and collection of this Indian crop begin early in April and continue till about the middle of December. The great bulk of the tea is imported here by the companies which grow it. There are many varieties of tea, the grades of which vary in quality and character to a very great extent. Of the various grades some are specially suitable for re-export, and others for different areas of the United Kingdom according to the varying tastes of consumers in this country.

The tea, after manufacture on the estate, is packed into chests which are despatched by the garden managers to the local port, where managing agents arrange for shipment to London. The Port of London Authority has many bonded warehouses specially for tea, and there are a number of others in London belonging to independent firms. On arrival of the consignment it is at once discharged from the steamer and transported to one of these warehouses, where it is weighed by the Customs officials and stored until the tea is sold and released for payment of duty. The agent of the tea estate receives weight notes and certificates, and when he has decided on the most favourable time to sell, he gives instructions to his broker to include the parcel in the public sales in Mincing Lane. At the same time he notifies the bonded warehouse so that the representative chests of each grade may be put out conveniently for sampling.

The centre of the world's tea trade is in London, about two-thirds of the total trade of the world being done with the United Kingdom market. Auctions of tea are held at the Commercial Sale Rooms in



Mincing Lane, and take place throughout the year on four days of the week, Mondays to Thursdays. The selling broker, who is entrusted with the disposal of the tea, compiles a weekly catalogue, in which the teas for sale are divided into convenient lots. To each of these a number is given, the name of the estate where the tea was grown, the quantity and description, the name of the warehouse where it is stored, and also the number of the tin in the broker's office in which is contained a sample of the particular parcel. Each catalogue also sets out in detail the conditions of sale, the date and time of the sale, and the "prompt" date. This latter is three months from the date of sale and is the latest date on which the buyer must make payment; in the meantime, the sellers are responsible for all storage charges, and should delivery be taken before the prompt date interest is allowed for the unexpired period.

These catalogues are issued to all the largest buyers and wholesale tea merchants, who send one of their assistants to the warehouses named to obtain a sample of the teas in which they are interested. The next step is for the prospective buyer to have the teas tasted by experts in order to estimate their values for his purposes, which are generally for blending. Most wholesale merchants run several qualities of tea, which it is necessary to keep up to a uniform standard. This cannot be done by always using teas from the same estate and in the same proportions, for the production of each estate varies during different parts of the year. It is therefore necessary to judge by tasting which teas, as they come on the market, will produce the requisite blend.

The immediate purchasers of most of the tea auctioned in Mincing Lane are the buying brokers. They number about a dozen and are members of the Tea Buying Brokers' Association of London. These act on behalf of the blenders and wholesalers at a commission of  $\frac{1}{2}$  per cent. The procedure at the sales is the same as that adopted at auctions generally, the bids are so much per pound, and the advances are by farthings. At the end of the sale the buyer applies to the selling broker for an order authorising him to draw at the bonded warehouse samples of the tea he has bought. These are compared with the original sample and, if inferior, the buyer can repudiate the sale. If, however, everything is in order, the selling broker sends out his advice note of the sales to the buyer and to the owner of the teas sold. These are now at the disposal of the buyer



to take delivery any time within three months, and warrants are issued in return for payment as deliveries are required.

• The tea is now in the hands of the wholesale merchant or the blender, who proceeds to prepare it for distribution. The tea is blended on a large scale and is distributed to the retailer either loose or, more frequently, in packets. The blender may also be part of a multiple shop organisation distributing the tea either through its own chain of retail shops, or through other shops as well. The great bulk of the tea thus distributed is sold in packets as a proprietary article.

### TEST PAPER XXXIII

1. Copy the diagram facing page 372 and explain the functions performed by the members marked in large Roman figures.
2. Classify the various members shown on the diagram facing page 372 as Collecting, Intermediary, and Distributing Traders.
3. Explain the function of the Collecting Trade, and name the persons who take part therein.
4. Indicate clearly the relation between the Intermediary Trader and the Centralised Market.
5. State three distinct classes of operations conducted by intermediaries engaged upon the produce exchange.
6. Enumerate the various channels open to the wholesale dealer engaged in the Import Trade for the disposal of his goods.
7. What is the function of the Distributing Trade?
8. Point out the chief differences in the services rendered by No. VI as compared with No. VII in the diagram facing page 372.
9. Name the members engaged in the Distributing Trade, and describe the nature of the services rendered by each.
10. Show clearly how an imported commodity may change hands at least eight times before reaching the consumer.
11. Imported foodstuffs are largely sold by auction, whereas raw materials such as wool are offered for sale in organised markets. Select a typical commodity sold in each of these ways, and explain how it eventually reaches the consumer.
12. Choose any imported commodity sold at a London produce exchange and trace the course it takes from its entry into an English port to its receipt by a consumer.



## CHAPTER XXXIV

### TRANSACTION IN THE IMPORT TRADE

As a rule, the shipping department of a mercantile establishment of any magnitude is a distinct branch, having its own chief, who is usually responsible for the business of his department. On their receipt by the office, all Bills of Lading for goods to arrive would be sent to this department, where they would be dealt with by the shipping clerk. The procedure followed with such documents and the goods they represent will now be considered, from the arrival of the goods at the docks until they are finally disposed of to some customer in the home market.

Let us suppose that Wilson & Co., Commission Agents, London, are importers of cocoa, and that they receive the following letter from Jones & Co., Boston, U.S.A.—

#### 1. Enclosing Bills of Lading

Messrs. WILSON & Co.,  
London, E.C.2.

15th April, 19\_\_.

Dear Sirs,

Confirming our letter of the 10th ult., we have now pleasure in enclosing Bills of Lading for 2,000 bags Cocoa, shipped per s.s. *Orama*, against Contract No. 271, dated January 15th.

Please pay the net proceeds into our account with Lloyds Bank.

Yours faithfully,

BEN JONES & Co.

#### 2. Acknowledging Receipt of Bills of Lading

Messrs. BEN JONES & Co.,  
U.S.A.

1st May, 19\_\_.

Dear Sirs,

We are in receipt of your valued favour of the 15th ult., enclosing Bills of Lading for 2,000 bags Cocoa against Contract dated 15th January, for which we thank you.

As requested, we shall pay over the net proceeds to your credit at Lloyds Bank.

Yours faithfully,

WILSON & Co.



The first step to be taken on receipt of the Bill of Lading is to ascertain when the vessel carrying the goods named on it is likely to arrive. This is done by inquiry at the office of the shipbroker, if the name of the broker is known ; or by keeping a careful watch in the shipping newspapers for the announcement of the movements of the vessel. On its arrival the goods are landed and taken charge of on behalf of the importer by one of the dock companies or wharfingers, and the consignment of cocoa is directed to one of the warehouses used for storing that class of commodity. These dock companies undertake the duty of weighing, measuring, gauging, sampling, etc., in accordance with the requirements of the various trades, for which purpose a large staff of experts and specialists is maintained. The preparation of the goods for sale having been completed with as much dispatch as possible, various accounts, known as "Landing Accounts," "Weight Accounts," "Piling Accounts," etc., are furnished to the importer, and samples are at the same time sent either to him or to some person authorised to receive them on his behalf. Specimens of a Landing Account and a Weight Account are shown on pages 380 and 381.

If the goods are not liable to Customs duty on importation, they are left at the disposal of the importer; after the examination by the Customs House officers has been made. On the other hand, if they are dutiable, as in the case of cocoa, all operations are jealously watched and guarded. The weighing is done in the presence, and under the actual direction and superintendence of an officer of Customs, and, in the case of tobacco, the actual manipulation of the weights is done by a subordinate official. The contents of the casks containing wines and spirits are measured by an official gauger. The weights and measures so taken are then recorded by the Customs officers, and these records become the official accounts of the goods, from which are compiled the returns made to the merchants, as named above.

The Landing Accounts having been received, the next step is to make arrangements for the sale of the goods, which is almost invariably done through the agency of a broker. Various classes of produce have their special markets, each of which forms the centre round which the brokers congregate when dealing in that particular class of goods.



65

-----*Royal Victoria*--Dock.

-----A-----Department.

-----June 27th-----19-----

## LANDING ACCOUNT

Of E.B., 1. 1092 Bags Rice-----

Entered by Wm. Anderson & Co.

on the 6th June 19  

Per the Ship County of Kent } Rotn. No.  
 Master Archer } 10747  
 from Calcutta }

Rent commences on the 17th July 19  

	cwt.	qrs.	lbs.
Tare — average —	0	2	26
each 20 Bags,			

Dock Nos.	Quantity.	Total Landing Weight.			
		Cwt.	qr.	lbs.	
<u>1</u> 1092	1092	2072	—	11	Gross
		42	—	23	Tare
		2029	3	16	Net

-----	-----	-----	-----
-----	-----	-----	-----
---J. Wilkins-----	Clerk.		
Examined---J. A. Albert-----			



## WEIGHT NOTE

Weights of G S I 1/90. 90 Bales Cotton, shipped per ss. "*Pandia*" to Liverpool by *Gaudia Cie, Porto Rico*.

Nos.		Tare	Nos.		Tare	Nos.		Tare	Nos.		Tare
1	3	25	31	3	25	61	3 1				
2	3	27	32	3	22	62	3	27	1/10	32	24
3	3	26	33	3	26	63	3	26	11/20	32	27
4	3	23	34	3	24	64	3 1 2		21/30	32	24
5	3 1	0	35	3	26	65	3	26	31/40	32	27
6	3	23	36	3	27	66	3	25	41/50	32	25
7	3	23	37	3	25	67	3 1 4		51/60	32	26
8	3	20	38	3	25	68	3	26	61/70	32	26
9	3	27	39	3	25	69	3	20	71/80	32	27
10	3	26	40	3	26	70	3 1 6		81/90	32	27
	32	24	15	32	27	15	32 1 26	15	Tare	290	1 9
11	3	26	41	3	25	71	3	23		12	0 6
12	3	22	42	3	27	72	3	26			
13	3	25	43	3	24	73	3	26			
14	3	26	44	3	26	74	3	25			
15	3	25	45	3	21	75	3	26			
16	3	24	46	3	26	76	3	24			
17	3	27	47	3	25	77	3	27			
18	3	26	48	3	23	78	3	25			
19	3	25	49	3 1	0	79	3	24			
20	3	25	50	3	24	80	3	25			
	32	27	15	32	25	15	32	27	15		
21	3	27	51	3	26	81	3	25			
22	3	20	52	3	23	82	3	22			
23	3	24	53	3	26	83	3	24			
24	3	24	54	3	24	84	3	27			
25	3	27	55	3	26	85	3	25			
26	3	23	56	3	27	86	3	26			
27	3	26	57	3	26	87	3	25			
28	3	25	58	3	23	88	3	24			
29	3	26	59	3	25	89	3	27			
30	3	26	60	3	24	90	3	26			
	32	24	15	34	26	15	32	27	15		



The letter giving instructions to the wharfingers to warehouse the goods would be sent as follows—

### 3. Instructions to Wharfingers

3rd May, 19\_\_.

Messrs. SMITH & Co.,  
Wharfingers, London.

Dear Sirs,

We enclose Bills of Lading for 2,000 bags Cocoa per s.s. *Orama*, which please enter for Cotons Wharf in our name.

Kindly draw the usual samples and forward to Messrs. Debenham & Co.

Thanking you for your kind attention to this matter,

We are, Yours faithfully,

WILSON & Co.

The 2,000 bags of cocoa having been placed in the warehouse, it is important that the importer should insure them against fire and theft whilst they remain in the warehouse, and, therefore, the insurance is effected with John Lloyds & Co., Insurance Brokers.

### 4. Effecting the Warehouse Insurance

4th May, 19\_\_.

Messrs. LLOYDS & Co.,  
Insurance Brokers, London, E.C.2.

Dear Sirs,

Please insure for us 2,000 bags Cocoa, marked B. J. & Co., value £17,000, against fire and theft whilst in warehouse for a period of one month.

We trust you will be able to effect the above at the lowest possible rate.

Yours faithfully,

WILSON & Co.

### 5. Advising the Placing of the Insurance

4th May, 19\_\_.

Messrs. WILSON & Co.,  
London, E.C.2.

Dear Sirs,

We thank you for your favour of even date, and in accordance



with your instructions we have to-day insured 2,000 bags Cocoa, value £17,000, against fire and theft whilst in warehouse for a period of one month.

We are pleased to say we have placed this insurance at 5s. per cent. and enclose debit note.

Yours faithfully,

LLOYDS & Co.

Instructions will then be forwarded to the produce brokers to dispose of the goods, and a letter similar to the following would be addressed to them—

#### 6. Giving Instructions to Produce Brokers

8th May, 19\_\_.

MESSRS. DEBENHAM & Co.,  
Brokers, London, E.C.3

Dear Sirs,

*Contract dated 15th January, 19\_\_.*

We beg to declare against the above, 2,000 bags marked B. J. & Co. of Cocoa shipped per s.s. *Orama*. Bills of Lading dated January.

Yours faithfully,

WILSON & Co.

At the "Commercial Sale Rooms," in Mincing Lane, sales are held daily of all sorts of Colonial and East Indian produce: teas, coffee, cocoa, sugar, spices, drugs, indigo, ivory, rum, jute, saltpetre, silk, and the numerous minor products of India and the East.

Again, the Corn Exchange, in Mark Lane, is devoted to the sale of all sorts of cereals and agricultural seeds; whilst the Baltic, in St. Mary Axe, is devoted to the sale of oil seeds and of the manufactured products of these seeds, such as oils and oil-cakes. The sales of wool are held at the Wool Exchange, in Coleman Street, where they take place at regular intervals. Green fruits are sold at Pudding Lane and Monument Yard, where the City fruit brokers have their sale rooms and offices. Covent Garden is also a large centre for the sale of this class of produce.

The samples drawn by the wharfingers are dispatched to the



sale rooms of the brokers in these various localities, and, in the present case, the samples of cocoa will be sent to the brokers, Debenham & Co., Mincing Lane. Here, they are inspected by the numerous buyers who frequent this special market.

The sales are usually by auction, the brokers taking care so to arrange their sales that one does not clash with another. At these auction sales, produce of fabulous value is bought and sold with a rapidity almost incredible to the uninitiated.

Having effected the sale of the 2,000 bags of cocoa placed with them, the brokers now send immediately to Wilson & Co. a **Contract Note**, setting forth all particulars of the goods sold, together with the price obtained for them; the terms on which they have been sold, and the date when the purchase is to be completed by the buyer paying for his purchase and receiving in return the necessary documents to enable him to obtain possession of the goods.

In the meantime, the importer has taken the necessary steps to obtain the "*Warrant*" for the goods housed with the Dock Company or other warehouse proprietor. This Warrant is a document of special value, since it represents the goods named on it, and, being transferable by endorsement, it is a simple and effectual method of completing a sale by handing it to the purchaser, as being equivalent to the articles he has purchased. When once a Warrant has been issued for goods, no delivery can be made from the warehouse where they are lying unless the Warrant, duly signed, is produced.

The 2,000 bags cocoa having been sold by the brokers, the following letter is next received by the importer—

#### 7. Asking for Delivery of Warrants

12th May, 19\_\_.

Messrs. WILSON & Co.,  
London, E.C.2.

Dear Sirs,

Kindly hand bearer Warrants for 2,000 bags Cocoa, Nos. 1 to 2,000, and oblige,

Yours faithfully,

DEBENHAM & Co.  
Brokers.



On receipt of this letter, the Warrants are endorsed to the purchaser of the goods, to whom they are now handed. The brokers also remit the proceeds, as seen from the following letter, together with *Pro Forma* Account Sales, showing all the necessary particulars of the merchandise sold, with the price obtained and the amount realised. From this latter amount they will have deducted any expenses incurred or paid on the goods and their charge for selling (i.e. "Brokerage"). Whatever remains is known as the "net proceeds," which are remitted to Wilson & Co. in the form of a cheque.

#### 8. Broker's Letter enclosing Remittance

14th May, 19\_\_.

Messrs. WILSON & Co.,

London, E.C.2.

Dear Sirs,

We beg to hand you herewith cheque for £15,564 12s. 10d. on account of sales of 2,000 bags of Cocoa, *ex* the s.s. *Orama*.

Your acknowledgment in due course will oblige,

Yours faithfully,

DEBENHAM & Co.

From the Account Sales on next page, it will be seen that four weights are given—

(1) Gross Weight, i.e. the weight of the goods and the bag which contains them.

(2) Tare, i.e. the ascertained or agreed weight of the package and packing.

(3) Draft, i.e. an allowance made to guard against any difference in weight which might occur between the time of the goods being weighed at landing and the date when the purchase is completed by the buyer giving payment for the goods.

(4) Net, i.e. the result after deducting Tare and Draft from Gross. It is upon this weight that the price is calculated.

On receipt of the brokers' Account Sales, the first duty of the importers is to subject it to critical examination. The weights are compared with the landing accounts, and the prices with the contract notes, and the various calculations are carefully checked to see that no errors have crept in or passed unnoticed in the



## 9. Commission Agent's Account Sales

Account Sales of B. J. & Co. 2,000 Bags Cocoa *ex s.s. Orama*  
from U.S.A. to London.

Sold on account of Messrs. Ben Jones & Co.

19----

	<i>cwt.</i>	<i>qr.</i>	<i>lb.</i>		<i>£</i>	<i>s.</i>	<i>d.</i>	<i>£</i>	<i>s.</i>	<i>d.</i>
2,000 Bags	4,000	0	0	gross						
	53	2	8	tare 3 lb.						
	3,946	1	20							
	35	2	24	draft 2 lb.						
	3,910	2	24	net at £4 cwt.	15,642	17	1			
				Disct. 2½%	391	1	5			
								15,251	15	8
CHARGES—										
Insurance on £17,000	.	.	.		42	10	0			
Entry and Stamps	.	.	.		1	2	0			
Dock Rates, Landing, etc., Dues.					125	0	0			
Freight on 200 tons; 30s. p. ton.					300	0	0			
Brokerage, ½% on £15,642 17s. 1d.					78	4	3			
Commission, 2½%	.	.	.		391	1	5			
								937	17	8
Net proceeds due	.	.	.					£14,313	18	0
E. & O. E. London	-----			19---						

brokers' office. The next duty is to prepare from the brokers' account an Account Sales, to be furnished to the original and actual proprietors of the goods, that is, Jones & Co., the exporters from the place of origin. This will be a transcript of the brokers' Account Sales, but, inasmuch as the home merchants will have paid a variety of charges and expenses upon the goods in the shape of Freight, Dock Charges, Marine and Fire Insurance, they will



add these items to the charges made by the brokers, and, after adding their own commission, will deduct this increased amount of charges from the gross proceeds of the sale, and will show the final amount of "net" proceeds which is to be credited to their correspondents. The transaction is closed by Wilson & Co. paying the sum of £14,313 18s. 0d. into the account of Jones & Co. at Lloyds Bank. Intimation of this step would be communicated to Jones & Co. as follows—

#### 10. Advising Remittance of Net Proceeds

16th May, 19\_\_

Messrs. BEN JONES & Co.,  
Boston, U.S.A.

Dear Sirs,

We beg to advise that we have to-day paid into your account with Lloyds Bank the sum of £14,313 18s. 0d., being the net proceeds of 2,000 bags of cocoa *ex* the s.s. *Orama*.

Assuring you of our best attention at all times and awaiting your further offers,

We are, Dear Sirs,  
Yours faithfully,

WILSON & Co.

In this example settlement is effected in a relatively simple manner by the importers, who pay the proceeds of the sale to the credit of a sterling account maintained by the exporters. If, however, the American firm required payment in their own currency the procedure would not be so straightforward. The English importers might settle by means of a bill of exchange, which the American exporters could discount with their bank, or some other form of bank remittance might be employed as described in the chapter on Foreign Exchange.

#### TEST PAPER XXXIV

From the particulars given below build up a transaction on the lines of the model given in the foregoing chapter—

Importers: Evan Jones & Co., New Street, Cardiff.

Shippers: Joseph Diaz & Son, Santos, Brazil.

Goods: 2,000 bags of Coffee.

Shipped: 20th June from Santos.

Ship's name: *Arizona*.

Port of arrival: London.

Mark and Numbers: ~~XXX~~ London.

Supply any further particulars to make the transaction realistic.



## CHAPTER XXXV

### CUSTOMS AND EXCISE

**THE CUSTOMS SERVICE.**—The primary business of this Government activity is the collection and management of duties of Customs and Excise in the United Kingdom of Great Britain and Northern Ireland.

The service is controlled from the Custom House in London, where the offices of the Commissioners of Customs and Excise are situated. For purposes of administration, the coast of the United Kingdom is divided into areas, which are each in charge of a Collector, who is responsible for the Customs work therein. Most of these areas contain a head port and, in addition, subsidiary ports and creeks. These subsidiary ports and creeks are in charge of officers of lower rank, subject to the Collector's supervision.

For convenience the Customs administration is divided into three main branches—

- (1) The Waterguard (or Preventive) Branch.
- (2) The Landing, Shipping, and Warehousing Branch.
- (3) The Clerical Branch.

The primary duty of the *Waterguard Branch* is the detection and prevention of unauthorised landings of uncustomed or prohibited goods by crews and passengers. The officers take account of the arrivals and sailings of vessels; meet and board vessels; take any necessary steps for the safety of the public health; deal with the dutiable stores of the crew and the vessel; and examine the personal effects of the crew and the baggage of passengers, and in most cases assess and receive any duty chargeable thereon. They visit and search vessels while in harbour, and watch shipping generally, with a view to the prevention of smuggling.

The work of the *Landing, Shipping, and Warehousing Branch* is mainly connected with goods which are (a) imported, (b) deposited in bonded warehouses, or (c) exported. The duty of the officers in connection with imported merchandise is to satisfy themselves that all goods borne on the "report" made by the Master of the importing ship are satisfactorily accounted for, and that all goods landed are duly "entered" in the appropriate form by the importer. The officers exercise control over the receipts and deliveries of goods at bonded









If Sailing Vessel  
or Steamer } *Steamer*

# REPORT.

No. 1 (Sale).

— Official Number *111004*

No. \_\_\_\_\_

Number of Register *10957*

Port of *Liverpool*

Date of Registry *10<sup>th</sup> Oct 1899*

Ship's Name	Tonnage	British or Foreign, if British, Port of Registry; if Foreign, Country to which she belongs	Number of Crew		Name of Master, and whether a British or Foreign Subject	Port or Place from which arrived.
			British Seamen	Foreign Seamen		
<i>Seal</i>	<i>900</i>	<i>Hull</i>	<i>25</i>	<i>Nil</i>	<i>J. Fisher</i>	<i>Bordeaux</i>
		TOTAL.....	<i>25</i>	<i>Nil</i>	<i>British</i>	

## CARGO.

1	2	3	4	5	6	7
Name or Names of Places where laden in order of time	Marks	No.	Packages and Descriptions of Goods, Particulars of Goods stowed loose, and General Denomination of Contents of each Package of Tobacco, Cigars or Snuff, intended to be imported at this Port	Particulars of Packages and Goods (if any) for any other Port in the United Kingdom	Goods (if any) to be transhipped or to remain on board for exportation	Name of Consignee
<i>Marseilles</i>	<i>OC</i>	<i>1/250</i>	<i>250 Btls Wine</i>		<i>In Transit</i>	<i>Order</i>
"	<i>SAD</i>	<i>184/1000</i>	<i>850 " Grapes</i>			"
"	<i>BEST</i>	<i>1/2250</i>	<i>2020 Casks</i>			"
"	<i>G</i>	<i>49/109</i>	<i>90 boxes Prunes</i>			<i>A. Jones</i>
"	<i>4m</i>	"	<i>276 keps Crowna Nuts</i>			<i>Estelle &amp; Co</i>
"	<i>RBC</i>	"	<i>216 cases Soap</i>		<i>In Transit</i>	<i>Order</i>
<i>Bordeaux</i>	<i>WS</i>	<i>1/100</i>	<i>100 Bags Rubber</i>			<i>Shin Mfg Co</i>
"	<i>SSE</i>	"	<i>70 Bales Horks</i>			<i>Order</i>
"	<i>VI</i>	<i>2/140</i>	<i>20 cases Vinegar</i>			"
"	<i>XXX</i>	<i>20/100</i>	<i>300 casks Rosin</i>			"
"	<i>JNO</i>	<i>1/10</i>	<i>10 cases Olives</i>		<i>In Transit</i>	"

If any wreck or derelict was taken  
in, or picked up, or taken  
aboard, or any casualty to the  
vessel occurred during the voyage,  
particulars to be stated

## STORES.

Surplus Stores remaining on board, viz	Tobacco, Cav.	lb	Spirits ... ..	galls	Sundry low duty goods }	
	" OS.	lb	Cordials or Liqueurs	galls		
	" unman.	lb	Perfumed Spirits	galls	Coal ... ..	tons
	Cigars	lb	Saccharin ... ..	oz.	Live Stock ... ..	

Number of Alien Passengers (if any) *British* *Foreign*

Pilots' Names \_\_\_\_\_

At what Station Ship lying \_\_\_\_\_

Agent's Name and Address \_\_\_\_\_

I declare that the above is a just Report of my Ship and of her Lading, and that the particulars therein inserted are true to the best of my knowledge, and that I have not broken bulk or delivered any Goods out of my said ship since her departure from the last Foreign Place of Loading.

I also declare that I have not landed aboard or transferred out of my said Ship any Goods shipped in the United Kingdom for use on board, except for the proper Export Duty on which will be paid within twenty-four hours.

(Signed)

Master.

Signed and declared this

day of

18

In the presence of

(Countersigned)

pro Collector.







warehouses and supervise operations on goods while in bond. They also examine goods from bonded premises presented for shipment.

The officers of the *Clerical Branch* deal with the receipt and payment of moneys and perform indoor clerical work. They receive and register the "reports" of masters of vessels arriving and issue "clearance" documents to masters of vessels departing.

**CUSTOMS.**—These are taxes imposed upon a commodity as it passes the frontier inwards or outwards. If the tax is imposed as the commodity enters the country it is an *import duty*; if it is taxed as it leaves the country it is an *export duty*. These taxes are among the oldest in history. Investigations have shown that among the earliest civilisations, such as the Babylonian, there were cases of Customs duties.

The British Customs duties for 1938 were found to yield nearly 264 million pounds, so that they form an important part of the revenue of the country. The law, as now embodied in the Customs Consolidation Act, 1876, and subsequent Acts dealing with particular commodities, requires that all persons concerned in bringing over to this country foreign goods of any description shall furnish definite information with regard to the same before the goods are landed. This information is of a twofold character, viz. the Ship's Report, and the making of the necessary entries.

**SHIP'S REPORT.**—The Master of every ship trading between a foreign port and this country is required to deliver a report, within twenty-four hours of arrival, of the whole of the cargo of his ship. Until this requirement is complied with, bulk is not to be broken, and no goods are to be landed. The chief points with regard to the Ship's Report are—

(1) The Report to be made on the prescribed form, as shown in the specimen inset.

(2) Particulars are to be furnished as follows: Name of ship, port of registry, nationality, master, port whence, number of crew, number of passengers (if any), whether British or alien.

(3) Particulars of the whole of the cargo set out in detail, such as—

<i>Marks.</i>	<i>Nos.</i>	<i>Description of Goods.</i>	<i>Landed or Transhipped.</i>
V5	365		
	400	36 Casks Wine.	Order or In transit, as the case may be.



Collector's No. and Date

## ENTRY FOR FREE GOODS

Collector.
Customs and Excise

This space is for the use of the officers of Customs.	Port of <i>London</i> Dock or Station, <i>Buttman Wharf</i> Importer's Name <i>C. Wray &amp; Co.</i>				Date of Report. <i>2/1/11</i>		Port or Place of Shipment of Goods. <i>Rotterdam</i>
	Ship's Name. <i>Alan</i>	Master's Name <i>A. Brown</i>	Rotation No. <i>36</i>	Examination.			
Marks and Nos. <div style="text-align: center;"> <i>Σ</i>  <i>C.M.W.</i> </div>	No. of Packages and Description of Goods in accordance with the Official Import List. <div style="text-align: center;"> <i>One hundred</i>  <i>bags Zinc</i>  <i>Oxide</i>  <i>Painters colours</i> </div>			Quantity. <div style="text-align: center;"> <i>cwts.</i>  <i>200</i> </div>	Value * <i>£ 215</i>	Name of place whence goods consigned. <i>Holland</i>	

I enter the above Goods as free of Duty, and declare the above particulars to be true.

Dated this *2nd* day of *January* 19..
 } (Signed) *C. Wray & Co.*  
*Importer or his Agent.*

\* (1) In the case of goods which are invoiced at a quoted price, the value to be stated in the Customs Entry should be the prime cost with the freight and insurance added ("c.i.f." value).

(2) When the goods are consigned for sale, the value to be given should be the latest sale value of such goods.



(4) When a vessel intends to discharge at several ports in the British Isles, a separate report is to be furnished relative to the goods to be landed at each port. Only goods thus *reported* can be landed at any particular port.

(5) The master is required to furnish an account of all stores liable to duty in the possession of himself or of his crew. Goods not duly reported are liable to detention and seizure (to be converted to the King's use) unless satisfactory evidence is forthcoming to prove that no fraud was intended. If the report is found to be false, the master is liable to a penalty of £100. (Customs Consolidation Act, Sec. 51.)

**ENTRIES.**—The importer, who may be the owner of the goods, or his accredited agent, is required, before his goods are landed, to declare and describe them in a document called *an entry*.

This description is to be in accordance with the requirements of the Import Tariff List.

(1) The entry is passed by the officers of Customs at the port of importation, and must agree with the record of the goods as contained in the report.

(2) Upon the production of this entry, the goods are allowed to be landed.

All goods are allowed to be landed except those prohibited by law to be imported. They must be entered and landed within twenty-one days from the date of the arrival of the ship, and are on no account to be removed, or in any way interfered with, prior to the Customs examination.

**CLASSIFICATION OF GOODS.**—The stage has now been reached when the goods have been removed from the ship and are awaiting examination and delivery. The subsequent procedure depends upon the nature of the goods. They may be classified broadly into two main groups, viz., Free Goods and Dutiable Goods.

**Procedure with Free Goods.** With free goods, the subsequent procedure is comparatively simple, and is as follows—

(1) The entry, known in this case as a "Free Entry," or "**Entry for Free Goods,**" is produced to the Customs officer where the ship is discharging. This entry should be made out in triplicate, and becomes the property of the Crown. The specimen on page 390 should be carefully studied.

(2) The goods are examined, and if the result of the examination



coincides with the particulars as set forth on the entry, the goods are passed as satisfactory.

(3) When the Customs authorities are satisfied that the requirements of the law have been duly observed, delivery of the goods is allowed.

No account of any goods can be taken by the Customs after the goods have passed from their charge, nor are the officers responsible for any damage to goods during examination. (Customs Consolidation Act, Sect. 76.)

**Procedure with Dutiable Goods.** With dutiable goods, the procedure is more complicated. The importer can choose from two courses which are open to him. He may either elect to pay duty *immediately on importation*, or elect to *warehouse the goods* in duly approved warehouses.

**Procedure when the Importer desires to pay Duty at once.** If the importer elects to pay duty on his goods, the following procedure must be observed—

(1) An entry must be passed giving the full description of the goods as to value, weight, and duty chargeable. This is known as an “**Entry for Home Use ex Ship.**” (See specimen, page 393.) It is passed by the Customs at the port of importation and the duty is paid at the time of passing.

(2) This entry, when duly passed and stamped to the effect that the duty has been paid, is forwarded to the officer at the dock or wharf where the goods are lying.

(3) The goods are examined. If the result of the examination agrees with the particulars on the entry, the goods are released. Should the weight of the goods, and, consequently, the duty chargeable, be found to exceed that declared in the entry, the additional duty must be paid before the goods can be delivered. If the reverse is the case, the excess duty is refunded to the merchant.

(4) When the officers are satisfied that the duty has been secured, and that all the requirements of the law have been duly observed, delivery of the goods is allowed.

When the goods are liable to a differential duty, varying according to strength, as in the case of wines and spirits; polarisation, as in the case of sugar; degree of sweetness, as in case of preserved fruits and condensed milk, *samples* are forwarded to the Government



# ENTRY FOR HOME USE EX-SHIP

Port of London Britannia Wharf  
 Importation  
 Name and address of Arthur Riggs & Sons  
 Merchant paying the Duty

(If Post) Prime Entry No.          dated 19  
 Master's Name Sty Martland Port or place of Shipment of Goods Rotterdam

Ship's Name Commodore Date of Report 3/3/

Marks and Numbers	Place and Country of destination in United Kingdom for Unmanufactured Goods and Spirits only.	Number of Packages and Quantity in Words and Description of Goods in accordance with the Official Import List.	Name of place whence Goods consigned.	Quantity in Figures	Value	a. d.
<u>A.R. 1/5</u>		<u>Five Casks</u> <u>Shall Stock</u> <u>Nine re 30</u> <u>Three hundred and fourteen Gallons</u>	<u>Holland</u>	<u>314</u>	<u>£63</u>	<u>19 18 3</u>

Total amount of Duty payable on this Entry £          19 18 3

I declare the above particulars to be true.  
 Date 4 March 19          (Signed) C Thompson  
 Importation Agent.  
 \* { (1) In the case of goods which are invoiced at a quoted price the value to be stated in the Customs Entry should be the prime cost with the freight and insurance added ("c i f" value).  
 { (2) When the goods are consigned for sale, the value to be given should be the latest sale value of such goods.



# ENTRY FOR WAREHOUSING

Port London Dock  
 Dock or Station  
 Importer's Name Chas. Hobbs & Co.

Ship's Name.		Date of Report.	Port or Place whence.		
<u>Albania</u>		<u>March 5<sup>th</sup> 19</u>	<u>Rio Janeiro</u>		
Marks and Nos.	No. of Packages	Description of Goods in accordance with the Official Import List.	Name of place whence Goods consigned.	Quantity.	Value £
<u>C.H.</u> <u>1/5</u>	<u>260</u>	<u>Bags of Coffee</u>	<u>Rio</u> <u>Janeiro</u>	<u>320 cwt</u>	<u>630</u>

I enter the above Goods to be Warehoused, and declare the above particulars to be true.

Dated this 6<sup>th</sup> day of March 19 { (Signed) E. Wright  
 Importer or his Agent.



Laboratory in order to ensure that duty is paid on the correct tariff rating.

**Procedure when the Goods are to be Warehoused.** On the assumption that the importer chooses the alternative described above, and elects to warehouse his goods, the procedure is as follows—

(1) A “**Warehousing Entry**” (see specimen on page 394) is passed at the Custom House. At the same time, a **Landing Order** relative to the goods is passed. The former is forwarded to the warehouse ; the latter to the dock or wharf where the goods are lying.

(2) Upon the receipt of the Landing Order, the officer at the dock allows delivery of the goods. They must be secured in a locked van with a Crown lock, or be accompanied by a Customs watcher (all at the merchant's expense).

(3) Upon being received at the warehouse, they are examined by the officer in charge and the account is taken. This being accomplished, the goods are legally warehoused, and the warehouse keeper is held responsible for their safe keeping.

**DELIVERY FROM WAREHOUSE.** When delivery of goods from the warehouse, either for home consumption or for exportation, is required, the procedure is for the merchant to prepare a “**Warrant**” (see specimen on pages 396-397). If the goods are for home consumption, this document will be composed of three parts—

(1) First portion will furnish particulars of goods. These will be checked by the Customs.

(2) Second portion will be a memorandum as to duty chargeable.

(3) Third portion will be a **Delivery Order** to the warehouse keeper.

If the particulars are correct, and when the duty is paid, the third portion (the Delivery Order) is forwarded to the warehouse, and the officer in charge allows the goods to be delivered.

When the goods are for exportation, the procedure is slightly different. A “**Warrant**” is passed as before, but the merchant has also to pass a “**Shipping Bill**.” This document furnishes particulars of the goods (marks and numbers), the name of the export ship, and where she is lying.

(1) The “**Warrant**” is composed of two portions only, there being no duty chargeable in this case. The first portion is retained by the Customs and the Delivery Order is forwarded to the warehouse.



## Kolo

## I. WARRANT—WET GOODS FOR. HOME CONSUMPTION.

No. —

Station -

Surrey Dock

**Notice is hereby given to deliver the undermentioned •**

9

Five baskets of  
blond hair  $\approx 30^\circ$

St Phillips  
Sons  
1914  
3917

Name of Firm paying duty

**Officer**

Date:

३  
१  
५

Received the sum of Twenty pounds,

	shillings and pence.	pence.
Twenty	Two	—

20.9.6

9  
.  
R  
.  
2

3 rod

1

3

Collector of Customs and Excise.



II. MEMORANDUM TO BE  
RETAINED BY COLLECTOR

Collector's No. \_\_\_\_\_ Date \_\_\_\_\_  
Station Surrey Dock  
Paid by A Phillips & Sons  
Description of Goods Wine

	£	s	d
Duty .. ..	20	2	6
Bottling charges ..	-	-	-
Total	20	2	6

C. and E. No. 495.  
Warehousing Code, paras. 496-505.  
Sec. 1947.

NOTE.—If the duty is paid on Gross Payment Receipts this Memorandum is not required and should be detached.

III. WAREHOUSEKEEPER'S ORDER.

Station Number \_\_\_\_\_  
Month and Year October 19

To the Warehousekeeper at Surrey Dock  
You may deliver the undermentioned goods, provided that they are actually removed from the Warehouse before any addition has been made to the duty chargeable.

Number and description of Packages and Goods to be warehoused	Builder's Name	Quantity and Unit	Mark	Measure	Duty of duty (to be paid to Warehousekeeper)
<u>Five Cases</u> <u>Clarret Wine</u> <u>net 30</u>	<u>A Phillips &amp; Sons</u>	<u>1914</u> <u>39.7</u>	<u>POS</u>	<u>1/5</u>	

A Phillips & Sons (Name of Firm)  
paying Duty.

Officer of Customs and Excise.

Date. \_\_\_\_\_



(2) The "Shipping Bill" is forwarded to the officer at the dock where the export ship is lying.

(3) Bond is required in all cases of exportation of dutiable goods, to cover the amount of the duty.

(4) When the officer furnishes a certificate of shipment on the Shipping Bill, the Bond is thereby cancelled. (A specimen "Shipping Bill" is shown on page 400.)

**TREATMENT OF GOODS WHOSE EXACT DESCRIPTION IS UNKNOWN.**

—The law subjects importers and their agents to severe penalties for false declarations as to the nature of the goods they import. It often happens, however, that the importer is not in possession of sufficient information to warrant his making an exact description of his goods for examination purposes. To meet this case, he may pass a document known as a "Bill of Sight."

This document gives all the information in the possession of the importer, and a declaration to the effect that such information is not sufficient to justify him in definitely entering the goods as dutiable or non-dutiable, as the case may be.

The Bill of Sight is forwarded to the officer at the dock or wharf where the goods are lying. The goods are thereupon examined, and the subsequent procedure depends upon the result of this examination.

(1) If the goods are not liable to duty, the Bill of Sight is perfected into a "Free Entry," and the goods are delivered.

(2) If the goods are liable to duty, the Bill of Sight is perfected to a "Prime Entry," and the duty paid. Delivery is then allowed.

Goods treated in this fashion usually include such articles as : tins of fancy biscuits, preserves of various fruits, scented waters, packages of books, clothing, with other goods liable to duty, etc. ; special preparations of medicines, paints, etc.

**GENERAL NOTES ON IMPORTATION.**—With regard to the administration of the Customs, the following points are of general interest—

(1) The Customs officials act as Public Health Authorities relative to the importation of various kinds of foods. All tea must be approved before it is admissible for consumption.

(2) The Merchandise Marks Act, administered by the Customs, provides against the fraudulent use of registered trade marks with a view to deceiving the consumers. Goods must be plainly



and indelibly marked with the country of origin, such as "Made in Germany," or with some other mark which leaves no doubt as to the country of origin.

(3) The importation of various articles is prohibited, e.g. obscene literature, lottery tickets, coin, matches with white phosphorus, gooseberry and currant bushes, hay, prison goods made abroad.

(4) Various restrictions govern the importation of other goods—explosives, live animals, etc.

(5) Goods can be landed only at places approved for the purpose. The list of approved docks, wharves, etc., is very large for London.

(6) Practically all tobacco, wines and spirits imported into the Port of London are warehoused. The proportion upon which duty is paid immediately on landing is exceedingly small.

**IMPORT DUTIES ADVISORY COMMITTEE.**—This is a Committee constituted for the purpose of giving advice and assistance in connection with the discharge by the Treasury of their functions under the Import Duties Act, 1932, which provides for the imposition of Customs duties on imported goods.

## EXCISE

**EXCISE.**—This word has been narrowed in its meaning in modern times. Formerly it had reference to any kind of tax upon any description of commodity, but now it is applied solely to a tax upon the production of an article within the country. Excise is a comparatively new tax, being invented about 1643 by the Long Parliament. It postulates production for a market and is imposed upon certain commodities which are produced in large quantities. Again, an Excise duty must be imposed to counterbalance the import duty on the same kind of goods or there would be a preference given to the home producer equivalent to a protective tax. If a tax be imposed on the importation of spirits and the home manufacturer be exempt, then the home production of spirits would be protected to the amount of the tax and the amount of imports would tend to decline.

Excise is now an integral part of our revenue system and the excise duties yielded over 106 million pounds for the year 1934.

Excise duties may be broadly classified as under—

(1) **DUTIES ON COMMODITIES.** Beer, Spirits, Wines, Glucose, Saccharin, Matches, etc.



\* Bruse  
the words  
that do  
not apply

# SHIPPING BILL FOR <sup>\*DRY</sup> ~~WET~~ GOODS AS MERCHANDISE.

Under Bond

Port or Collection District Station	<u>London</u> <u>Surrey Dock</u>	Station No.	
Month and Year	<u>August 1911</u>		
Export Ship	<u>Boragon</u>	Master	<u>Henry Fraser</u> for <u>Brockholm</u>
Entered Outwards	<u>4<sup>th</sup> August 19</u>	Bond given	<u>2<sup>nd</sup> August 19</u>
Station		Lighterman	<u>Bugden</u>
Conveyance	<u>Lighter</u>	<u>Carmen</u>	
		<u>A. Rendall</u>	Exporters or Agents
		<u>19 St James St. E.C.</u>	Address

Shipping Marks and Numbers, Final Destination and name and address of the Consignee	Number of Packages	Description of Packages	Description of Goods	Quantity				Country whence goods were consigned when imported	Rate of Draw back (if any) allowed	Value
				Wet Goods Gallons, &c.	Dry Goods cwt. qrs. lbs.					
F. D 7/s	Five Cases		N.B.—These goods must be produced to the Officer of Customs and Excise at time of Shipment, and any Short-Shipment notified  Burgundy Wine nr 30°	Nine gallons				France		£17
TOTAL			Hy Philips Sons 16 Gale St. London E.C.							Officer. Date.



(2) **LICENCE DUTIES.** These duties are generally payable when persons are licensed for the sale of commodities, and are divided into two main divisions—

(a) *Liquor Licences.* Distillers, brewers, rectifiers and compounders, wine manufacturers, wine, beer and spirit dealers and retailers (publicans), clubs, etc.

(b) *Other than Liquor Licences.* Motor spirit dealers, methylated spirit retailers, tobacco manufacturers and dealers, hawkers, pawnbrokers, auctioneers and appraisers, patent medicine vendors, refreshment houses, plate dealers, vinegar makers, theatres, etc.

**COMMODITIES SUBJECT TO EXCISE.**—The following are subject to Excise Duties—

**DISTILLERIES.** One of the principal items of Excise revenue is the duty on British spirits. The duty at present is 72s. 6d. per gallon. The spirit is manufactured at the various distilleries in the Kingdom, and is subjected to strict Excise supervision at every stage in the manufacture. The spirit, when manufactured, is warehoused at the Distillery Warehouse, and the procedure when delivery is required is similar to that when dealing with Customs Warehouses.

A proportion of the spirit thus produced is used for the manufacture of methylated spirits. The pure spirit is mixed with certain proportions of wood naphtha, if industrial methylated spirit is required, and wood naphtha with mineral naphtha, if the mineralised variety is required. The alcohol thus disposed of is free of duty. The manufacture of methylated spirits is under Excise control.

**BREWERIES.** The other main item of Excise revenue is the duty on beer (100s. per barrel of 36 galls. of a specific gravity of 1055°). The duty being considerably less than on spirits, the Excise supervision is less rigid as a consequence. The whole process is supervised by the Crown officers at the various breweries.

The duty is paid at the end of every month, and no beer is warehoused in Bonded Warehouses, as is the case with wines and spirits.

**GLUCOSE.** Various glucose factories exist and are under Excise survey.

**BRITISH WINES.** There are only a few manufacturers of British wines subject to Excise survey.

**SPIRITS.** The only commodity which is, in the real sense,



subject to continued Excise control consists of **British spirits**. All British spirits must be disposed of in one of the following ways—

- (a) For Home Consumption ;
- (b) Methylation ;
- (c) Exportation.

**Home Consumption.** In the case of home consumption the procedure is as follows—

(1) The casks, immediately on being filled from the distillery, are warehoused in the distillery warehouses. When all the particulars are taken, the merchant fills up his "*Removal Warrant*." This document sets forth the contents of the cask and the strength of the spirit.

(2) The casks may be removed to a rectifier or compounder. Only "*Duty Paid*" spirits are thus allowed to be disposed of. They cannot be removed from the distillery, even after duty has been paid, until an *Excise Permit* is granted. This document accompanies the goods to their next destination.

(3) The spirits are rectified and compounded (i.e. flavoured, sweetened, etc.). All rectifiers and compounders are subject to Excise supervision. Before the goods can be removed, another Excise Permit is granted, and accompanies the goods as before.

(4) The spirits are now removed to a spirit dealer, who is duly licensed to receive spirits. A spirit dealer is not allowed to sell less than 2 galls. of spirit in any one consignment. An Excise Permit must again accompany the goods.

(5) The spirit dealer now forwards the spirits to the spirit retailer or publican. He is duly licensed, and is not allowed to sell more than 2 galls. in any one consignment. An Excise Permit again accompanies the spirit.

The important point to remember is that all spirits, even when "*Duty Paid*," must not be removed either from warehouse to dealer, or from dealer to retailer, unless accompanied by an *Excise Certificate*. These persons are liable to be challenged at any time by a Crown officer, and unless this Certificate is produced, the goods are liable to seizure.

**Methylation.** A proportion of the spirit produced is used in methylation. The spirit is removed to the methylators under Bond and accompanied by a Permit. The spirit is mixed with mineral and wood naphtha in the presence of an Excise officer.

When the methylated spirit is sent out to the dealers or retailers



it must be accompanied by a Certificate. These Certificates are inspected every quarter.

**Exportation.** The procedure is almost identical with that followed by the Customs in dealing with the exportation of goods.

**DRAWBACK.**—This is the sum paid back by the Government upon certain classes of goods exported on which duty has already been paid. Drawback goods consist chiefly of two classes—

(a) Goods manufactured in the United Kingdom on which Excise duties are paid, such as spirits and malt liquors ; and

(b) Those composed of raw material which has paid Customs duty on importation, such as snuff, manufactured tobacco, and cigars. Neither Customs nor Excise duties are payable on goods which are not consumed within the United Kingdom, and therefore it is necessary to make provision for the repayment of duty which has already been paid under either of these heads.

To secure this repayment or drawback, notice must be given to the Revenue officers of the intention to export any such goods, which are then placed in charge of the Customs officers in attendance upon the exporting ship. A note is prepared and signed as in the case of bonded goods ; and on production to the proper officers—either of Customs or of Excise—of the certificate of exportation, a document known as a debenture is handed to the exporter, and this authorises the repayment of the amount of duty.

**BOUNTIES AND SUBSIDIES.**—These constitute a method by which governments have encouraged the production and export of goods. The policy, far from being a new one, was an integral part of the mercantilistic system of trade regulation, though, during the nineteenth century, it fell into disuse, so far as Great Britain was concerned. In recent years, however, and particularly since 1931, it has been employed on an increasing scale.

A *bounty* has been defined as the payment by the State of a definite sum per unit of commodity produced or exported. A *subsidy*, on the other hand, is a payment by the State on any other basis, for example an annual lump sum payment. In current literature, the two terms are used interchangeably. Sometimes a subsidy is granted upon the condition that some service shall be rendered to the State, as for example the subsidies to steamship lines which have been made on the condition that they should maintain special services for the carriage of mails. In such cases,



the real subsidy consists in the excess of the payment received over the cost of rendering the service to the State—a sum which it is probably impossible to calculate with any degree of accuracy.

British subsidies prior to the outbreak of the Second World War were designed to help the home producer rather than to stimulate exports. The tramp shipping subsidy would give some indirect assistance to exporters, whilst a coal export subsidy was under discussion but was never introduced. The policy was most widely used in order to assist certain branches of agriculture.

### TEST PAPER XXXV

1. What are Customs duties and for what purposes are they levied?
2. What information must be furnished by a person importing foreign goods into this country?
3. Explain the nature of the Ship's Report.
4. State clearly the use of the document known as an *entry* in connection with imported goods.
5. Into what two groups may imported goods be classified?
6. If a consignment of fruit were sent to you, what entry would you have to pass before obtaining permission to remove the goods?
7. Mention the two alternatives open to the importer when dealing with dutiable goods.
8. How would you clear dutiable goods intended for immediate home consumption?
9. A merchant receives a consignment of dutiable goods which are not required for immediate use. What entry is he required to make in such a case, and what steps would he take to obtain delivery of the goods when they are required for use?
10. An importer of foreign goods has to "declare" the consignments he receives. What is meant by "declaring" goods and how is it done? What is the procedure followed by an importer to obtain possession of dutiable goods?
11. When goods are imported with the intention of being re-shipped to another country, is it necessary to pass any Customs entry?
12. Describe the treatment of imported goods whose exact description is unknown.
13. Mention any goods whose importation into this country is prohibited.
14. What is the difference between Customs Duties and Excise Duties?
15. Give a broad classification of Excise Duties.
16. Enumerate some of the most important commodities which are subject to Excise.
17. Explain the meaning of the terms "Drawback," "Bounties," and "Subsidies."
18. Distinguish between specific and *ad valorem* duties. If goods which had paid customs duty on entering this country are subsequently exported, can the trader recover the duty paid? If so, state the procedure.



## CHAPTER XXXVI

### ORGANISATION OF THE EXPORT TRADE

**INTRODUCTION.**—In opening up a new market for his goods in a foreign country, the intending exporter should first make investigations into the following points—

(1) The financial and political conditions prevailing in the country to which the goods would be exported.

(2) The extent of the needs for the commodities in question, together with the purchasing power of the probable consumers.

(3) The conditions of sale.

(4) The terms of payment and the nature of the banking facilities.

(5) The Customs duties and the question of consular invoices ; also into the manner in which the Customs officers treat the packing when examining whether the goods are or are not dutiable.

(6) Any legislation concerning the manufacturer's trade marks and the method of litigation in case of non-payment.

(7) The method of procedure in entering into business relations with intending customers.

(8) Any particulars relative to the goods which he proposes to export, such as qualities and quantities consumed, selling price, kinds of packing, existing competition, etc.

Unlike the custom prevailing in the home trade, the dominating factor in the export business is trade on *commission*, direct sale being very rare, although there are many attempts to develop it.

**EXPORT ON CONSIGNMENT.**—The method adopted in early days was that of *consignment*. The manufacturer forwarded to the commission agent a quantity of goods, and the latter did his best to dispose of them in the interests of his principal. The proceeds of the sale were remitted to the principal after the deduction of the expenses incurred. However, trade on consignment tends more and more to disappear. It is necessary to keep in constant touch with the consignee and to repose in him an unlimited confidence. Sometimes the consignee is tempted to abuse this confidence by the neglect of his engagements, by understating the amount he has actually received for the goods, or by submitting an exaggerated statement of his expenses. There are also other



risks. The market prices might undergo a serious alteration during the transport of the goods, and a consignment calculated on a basis from which a profit was anticipated would then be converted into a loss. Finally, the methods of communication have improved, so that it is no longer necessary to maintain huge stocks at overseas depôts for the convenience of purchasers. Orders can now be so executed as to spread the delivery of the goods over a certain period.

**MEMBERS ENGAGED IN THE EXPORT TRADE.**—A large proportion of the goods manufactured in the British Isles is exported to foreign countries in exchange for food-stuffs and raw materials. On account of the essential difference in the nature of the imports and exports, the present organisation of the British export trade, which is concerned mainly with manufactured goods, differs materially from the import organisation. The form taken by the export organisation is illustrated by the diagram on page 407.

From this diagram it will be seen that, generally speaking, the following members take part in the export of goods, say, from England to India—

- (1) The Manufacturer.
- (2) The Firms engaged in the collection of the goods from the Manufacturer.
- (3) The Wholesale Merchant or Commission Agent engaged in the Export Trade.
- (4) The Agent in the foreign country (i.e. India).
- (5) The Importer in India.
- (6) The Wholesale Merchant.
- (7) The Retail Dealer.
- (8) The Consumer in India.

Each of these members has his definite function to fulfil, according to the extent to which the principle of division of labour has been carried, and according to the magnitude of the transactions undertaken. Since these functions are not entirely different from those of the corresponding members in the import trade, it will be sufficient here to explain the special duties of the exporter in England and the importer in India.

The export of goods is undertaken by three different types of trader—

- (1) The *Commission Agent* who acts as buyer for merchants

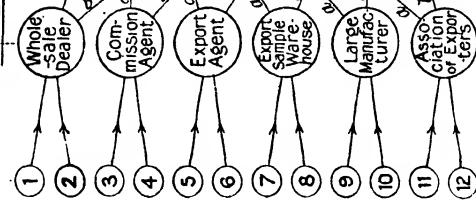


# EXPORT OF MANUFACTURED GOODS

## ENGLAND.

### I. MANUFACTURER

#### II. BUYERS



### III. EXPORTER

(Wholesale Dealer or Commission Agent.)

Exporter

For-warding Agent

A

A.Auxiliary to the Exporter

### IV. AGENT

Abroad

Agent in India

For-warding Agent

A

A.Auxiliary to the Exporter

## INDIA.

### V. IMPORTER

Importer

Importer

Whole-sale Dealers

Whole-sale Dealer

Commission Agent

For-warding Agent

B

B.Auxiliary to the Importer

### VI. WHOLESALER

Whole-sale Dealers

Whole-sale Dealer

Commission Agent

For-warding Agent

B

B.Auxiliary to the Importer

### VII. RETAILER

Retailer

Retailer

Retailer

Retailer

Retailer

Retailer

Retailer

Retailer

Retailer

Retailer

Retailer

Retailer

Retailer

Retailer

### VIII. CONSUMER

Consumer

Consumer

Consumer

Consumer

Consumer

Consumer

Consumer

Consumer

Consumer

Consumer

Consumer

Consumer

Consumer

Consumer



abroad. On receipt of an indent from his principal, he orders the goods from manufacturers at home, and then ships them under his own invoice.

(2) The *Wholesale Merchant*, who exports his own manufactured goods to buyers or branch houses abroad.

(3) The *Forwarding Agent*, whose operations are usually restricted to the receipt, packing, and forwarding of goods sent to him by different traders in this country.

**The Commission Agent.** The commission agent engaged in the export trade acts as a direct buyer of manufactured goods in the entire sphere of his purchasing area. He acts in his own name, but for the account of either the foreign buyer or importer or on behalf of the home manufacturer. For instance, an English commission agent may receive an indent for various kinds of goods from a buyer in India. His first duty would be to obtain from the various makers their prices for the goods and the time required for their delivery, and on receipt of these particulars he would place his order with the firms offering the best terms. Thus, he would be acting as intermediary between the home manufacturer and the Indian buyer. Again, the English manufacturer might induce the commission agent to export a consignment of his goods to some district in India, in the hope that there would be a demand for them at profitable prices. In this case, the commission agent would be acting on behalf of the English manufacturer, and not for the Indian buyer.

The commission agent engaged in the export trade must have a special knowledge of the goods in which he deals. He must not only understand the various kinds and qualities of the articles produced, but must keep in close touch with the movements of their prices and with any alterations which take place in the process of their production. His next duty is the linking up and gradual extension of his business connection with foreign buyers, and the application of the best methods for facilitating the sales. The essential conditions for the attainment of this end are to be found in the residence in the foreign country for many years, in the wise selection of agents, the opening up of business relations with other commission agents, and the establishment of foreign branches and places of sale. The primary object of the commission agent is naturally to obtain orders or indents from foreign



buyers, and then to pass them on in his own name to the home manufacturers. Moreover, he has to supervise the execution of these orders and bring them to a satisfactory conclusion.

In his dealings with the manufacturer, the commission agent acts in the interests of his principal (i.e. the foreign buyer), and insists on the goods being made according to sample, and on the date fixed for delivery being adhered to. He also effects the work connected with the dispatch of the goods, such as the arrangements with the shipowner, the preparation of the Bill of Lading, the procuring of the Customs documents, the effecting of insurance, etc. In his dealings with the foreign buyer, the commission agent acts in the interests of the manufacturer with regard to the fulfilment of the contracts, the receipt of the goods, and the payment for them.

Thus, the commission agent engaged in the export trade places at the service of the two parties brought together in his name, not only his trade organisation, his experience and knowledge acquired in the course of many years, but also the reputation and good name of his house. More than this, he represents both parties with his capital and his credit, and bears many risks which will be alluded to in a later chapter.

**The Wholesale Export Merchant.** The wholesale merchant engaged in the export trade performs practically the same services as the export commission agent, except that he concludes the purchase and sale of the goods for his own account, and derives his profit from the difference between the purchase and the selling price of the goods. On the other hand, the commission agent draws a fixed commission, to which may be added, by arrangement, certain increments due to the fluctuation of the exchanges, discounts accorded to him by insurance and shipping firms, etc.

**The Forwarding Agent.** The duty of the forwarding agent differs from that of the above two members of the export trade, in that he is not usually entrusted with the buying of the goods. The orders are sent direct by the customer abroad to the English trader or manufacturer, and in payment the latter usually receives a direct remittance.

On the employment of a forwarding agent, the English manufacturer supplies him with an *Advice Note* containing instructions relating to the goods which are to be consigned. In case the



MANCHESTER,  
28<sup>th</sup> Nov., 19.....

Forwarding Instructions for Sender & Co., Forwarding Agents,

10 and 12 Tower Street, London, E.C.3.

Forwarded to you to-day, by rail, the goods below specified. Kindly forward same at the agreed rate and terms.

*John Brown.*

Marks.	Numbers.	Numbers and Description of Package.	Contents.	Weight in Cwts.	Value for Insurance.	Value for Customs.	Consignees.	Place of Destination.	Observations with regard to Prepayment.	Way of Conveyance.
J.B.	1516	1 case	Coloured Wooden Toys	5	—	£3 15 0	René Fonzes	Lyons	free of charge	—
—	1517	1 do.	do.	5	—	£6 15 0	A. Petit	Lille	do.	—



goods are dispatched from a place in which the forwarding agent has neither a representative nor any organised system of conveyance, they are addressed by the manufacturer to the forwarding agent. The latter, on taking possession of the goods, attends to their freighting in accordance with instructions; executes all necessary shipping formalities, such as the preparation of the Bill of Lading, Customs declarations, etc. The goods having been dispatched, he has next to send instructions and documents to the forwarding agent abroad, if such a person be employed. If the forwarding agent has also to effect the insurance, he fills up the necessary proposal form, forwards it to the insurance company, and receives the policy in return. Sometimes the forwarding agent himself is the representative of an insurance company: in that case, the insurance begins to operate immediately it has been entered in the register kept for that purpose.

**THE IMPORTER.**—The foreign importer may be a separate person or firm, or a person in partnership with the exporter. His work is not less difficult than that of the exporter, since it is his duty to direct the sale for a wide area from his particular centre. He must have a good knowledge of the requirements of the native consumer or of the people residing in his selling area, and must post his indent or order in good time so that he will be in possession of the goods when they are required. Further, he has to effect all work connected with the receipt of the goods, such as the checking of the goods, the upkeep of the warehouse, and the execution of the sale, as well as other matters incident to the transactions. Moreover, the importer must also place his capital and credit in the service of his undertaking; and must bear a number of risks, even though he is conducting the business, not on his own account, but as commission agent in the service of the English exporter or manufacturer, or even on account of the wholesale merchant or retailer in his own country.

**RISE OF THE EXPORT AGENT.**—In addition to the functions performed by the above principal members, there are also a number of particular services to be rendered in the export trade by special representatives of the commodity; and especially where the importation of the goods is effected without the aid of an exchange, as usually in the case of ready-made goods. Of recent years in this connection there has been enlisted the services of a special



trader known as an *Export Agent* (see diagram), whose duties are similar to those of the wholesale export merchant, since he represents the home manufacturer. As a rule, sample rooms are kept by the export agent in the chief exporting centres, which facilitate the exporter in his selection of goods and in his giving of orders, as well as saving him the trouble and expense of making journeys to the places of manufacture. These sample rooms, which are sometimes known as Export Museums, may be organised directly by the manufacturers, whose aims are then similar to the dairy farmers who provide themselves with a selling association, or similar to that of the wholesale salerooms in Manchester in connection with the co-operative distributive societies.

**CONCLUSION.**—As the commission agent and wholesale merchant engaged in the export trade are in co-ordinate relationship to each other, it will be found from a study of the diagram on page 300 that there are usually six persons involved in the exportation of manufactured goods. In addition to the manufacturer and the consumer, there are—

- (1) The Exporter (No. III).
- (2) The Importer (No. V).
- (3) The Wholesale Merchant (No. VI).
- (4) The Retailer (No. VII).

Thus, the goods generally pass through four different hands in the course of their distribution, and are subject four times to an increase in price. In the case of manufactured goods, this additional increment to the cost of the goods is greater in proportion to the magnitude of the labour and risk involved than in the case of the importation of raw materials. It is, therefore, natural that in the exportation of manufactured goods, there is a tendency to eliminate the middleman wherever possible.

### TEST PAPER XXXVI

1. Enumerate the chief members engaged in the Export Trade.
2. Copy the diagram on page 407 and explain the function of each of the members marked in Roman figures.
3. Describe the work of the Commission Agent engaged in the Export Trade.
4. In what respect does the Wholesale Export Merchant differ from the Commission Agent engaged in the Export Trade?
5. Explain carefully the services rendered by the Forwarding Agent in the Export Trade.
6. Compare the duties of the exporter with those of the foreign importer.



## CHAPTER XXXVII

### TRANSACTIONS IN THE EXPORT TRADE

THE chief stages through which an export transaction has to pass are as follows—

- (1) The receipt of the indent from abroad.
- (2) The placing of the orders contained in the indent.
- (3) The packing and forwarding of the goods.
- (4) Shipping the goods.
- (5) Effecting the insurance.
- (6) Invoicing the goods.
- (7) Drawing Bills of Exchange against shipment.

**RECEIPT OF INDENT FROM ABROAD.**—The first step in an export transaction is the receipt from abroad of the merchant's indent or order for goods which he requires to be shipped to him. The particulars usually provided by an indent are—

- (1) Details of the goods required.
- (2) The price.
- (3) Packing and shipping instructions.
- (4) Date of shipment.
- (5) Method of reimbursement.

Indents are, naturally, of the most varied character, and deal with such goods as hardware from the Midlands, cotton from Lancashire, pottery from Staffordshire, cutlery from Sheffield, woollens from Yorkshire, and the numerous other productions of our factories and workshops, besides iron, steel, coal, coke, salt, cement, and other partly or wholly manufactured goods of the rougher sort. In addition to these British manufactures, the Continent is often called upon to supply wines and spirits, perfumery, fancy goods, silk, woollen stuffs, watches, jewellery, toys, and innumerable small wares which Continental workmen turn out so tastefully and cheaply.

On page 414 is a copy of a simple indent received from Messrs. J. Edwards & Co., of Demerara, by George Penny & Co., Commission Agents, London.

**PLACING OF ORDERS.**—Messrs. Penny & Co. first dissect the indents they receive so that the orders for the various goods mentioned in them can be properly placed with the manufacturers



## 1. Receipt of Indent

INDENT No. 50.


*Demerara,*

-----19

Messrs. GEORGE PENNY & Co.,  
London.

Please purchase and ship to us by an early steamer of the ----*R.M.S.P.*---- Line, the goods named below. You will insure them for the amount of your Invoice, adding ----10----% for imaginary profit, and for your reimbursement, please draw on us in favour of the ----*Colonial*---- Bank, with which we have arranged that your Draft on us, with documents attached, shall be accepted as cash, discount and premium being placed to our account.

*J. Edwards & Co.*

Marks, etc.	Description of Goods.	Remarks.
 Demerara	1,000 barrels Potatoes, each about 1½ cwt. net, at lowest possible price.	

and wholesale dealers who are best able to supply them. The above indent contains but one item, viz., 1,000 barrels potatoes, and the commission agent will probably inquire for quotations of several firms prior to placing the order. The letter asking for a quotation would read as follows—

## 2. Asking for a Quotation

LONDON,  
19..

Messrs. RICHARD WATSON & Co.,  
Potato Merchants,  
Arran Road, E.3.

Dear Sirs,

Please quote us your very lowest price f.o.b. London for 1,000 barrels potatoes, each about 1½ cwt. net, for prompt shipment to Demerara.

Yours faithfully,

GEORGE PENNY &amp; Co.



A similar inquiry would be sent to other firms, say, Messrs. E. MacDougall & Co. and Messrs. J. Abbott & Co.

The selection of goods, or buying, is a matter in which practice varies a good deal. In some houses one or more buyers, knowing both home and foreign markets, are employed; in others, the partners of the firm undertake the duty, with the occasional assistance of their senior clerks; whilst in others the selection is practically left to agent or packers in the various towns and cities, to whom the orders are sent, and who make all the necessary purchases and arrangements, charging a small commission for their trouble.

There are, of course, many kinds of goods in which no special selection is necessary, or which can be ordered from sample, brand, or trade mark, such as wines, spirits, beer, soap, candles, pickles, sauces, jams, salt, scrap pig or other iron, biscuits, potted and canned meats and fish, in all of which a very extensive export trade is done.

The replies to the inquiry for quotations for potatoes may be as given below, from which it will be seen that the lowest quotation is that received from Messrs. J. Abbott & Co., viz. 8s. 6d. per barrel, f.o.b. London.

### 3. Quotation given

MESSRS. GEORGE PENNY & CO.,

127 Walden Road, E.C.2.

Dear Sirs,

Replying to your esteemed inquiry, we can quote you 8s. 9d. per barrel f.o.b. London, and should be glad to receive your orders, to which we would give our best attention.

Yours faithfully,

RICHARD WATSON & CO.

### 4. Quotation given

MESSRS. GEORGE PENNY & CO.,

127 Walden Road, E.C.2.

Dear Sirs,

In reply to your inquiry, we offer you potatoes in barrels of about  $1\frac{1}{2}$  cwt. net at 9s. 3d. per barrel f.o.b. London, and hope to receive your esteemed order.

Yours faithfully,

E. MACDOUGALL & CO.



**5. Quotation given**

Messrs. GEORGE PENNY & Co.,  
127 Walden Road, E.C.2.

Dear Sirs,

We have your inquiry, for which we thank you. In reply, we can offer you the potatoes specified at 8s. 6d. per barrel f.o.b. London.

Yours truly,

J. ABBOTT & Co.

In reply to the quotation made by Abbott & Co., it is assumed that a further communication is addressed to them containing a counter offer of 8s. 3d. per barrel.

**6. Making a Counter Offer**

Messrs. J. ABBOTT & Co.,  
1 Wray Street, E.4.

Dear Sirs,

We thank you for your quotation, which we have carefully considered, and are willing to give you an order at 8s. 3d. per barrel for 1,000 barrels potatoes each about  $1\frac{1}{2}$  cwt. net, f.o.b. London, we to have the opportunity of inspecting them before shipment. We enclose our order sheet No. 3045 and trust that you will be able to accept our offer.

Yours faithfully,

GEORGE PENNY & Co.

ORDER.

No. 3045

From George Penny & Co.

To Messrs. J. ABBOTT & Co.,

1,000 barrels Potatoes each about  $1\frac{1}{2}$  cwts. net, at 8s. 3d. per barrel net, f.o.b. London, everything included. If on our inspection the goods are found to be unsuitable, we to have option of rejecting them.

The acceptance of the counter offer completes the contract



between the parties, and would be embodied in a letter similar to the following—

#### 7. Accepting the Counter Offer

MESSRS. GEORGE PENNY & CO.,  
127 Walden Road, E.C.2.

Dear Sirs,

We beg to acknowledge receipt of your favour enclosing your order sheet No. 3045 for 1,000 barrels potatoes at 8s. 3d. per barrel. We have gone into our figures again very carefully and while this figure leaves us scarcely any margin, we will accept your offer for the sake of future business. We shall be packing early next week and you may call at our warehouse any time to inspect the potatoes. Kindly let us have your forwarding instructions, and oblige,

Yours faithfully,

J. ABBOTT & CO.

**PACKING AND FORWARDING GOODS.**—The order having been placed, full directions as to the marks and numbers to be put upon the barrels would be furnished to Messrs. Abbott & Co., together with the name of the port, dock, or goods station to which the goods are to be sent, as well as the name of the ship by which they are to be shipped and her destination. The letter furnishing these particulars would read thus—


#### 8. Giving Forwarding Instructions

MESSRS. J. ABBOTT & CO.,  
1 Wray Street, E.4.

Dear Sirs,

We thank you for your favour and note that you accept our offer. We shall be down early next week to inspect the potatoes.

You will please have these dispatched, as they are packed, to Shed 13 at the South West India Docks for shipment per s.s. *Pergon*, which is receiving cargo until the 27th inst; barrels to

be marked: . Kindly let us have your invoice, with  
Demerara  
weights, etc., as soon as possible.

Yours faithfully,

GEORGE PENNY & CO.



The following letter would be forwarded to Messrs. J. Edwards & Co., Demerara, by the commission agents in London—

### 9. Intimating the Execution of Indent

Messrs. J. EDWARDS & Co.,  
Demerara.

Dear Sirs,

We beg to confirm our last per s.s. *Aurelio*, and have since received your kind order dated 12th ult. for 1,000 barrels potatoes. We are pleased to say we have succeeded in buying these at 8s. 3d. per barrel f.o.b., and contemplate shipping per s.s. *Pergon*, which is sailing about the 30th inst.

Assuring you of our best attention at all times,

We are, Yours faithfully,

GEORGE PENNY & Co.

The order having been given out and arranged by Penny & Co., commission agents, in due time the advice that the goods are being sent forward will be received, and the invoice will come to hand as follows—

### 10. Merchant's Invoice to Commission Agent

WRAY STREET,  
LONDON, E.4.

INVOICE.

Messrs. GEORGE PENNY & Co.,  
E.C.2.

To JOHN ABBOTT & CO.

Dr.

Potato Merchants.

To 1,000 barrels Potatoes each about 1½  
cwts. net. at 8s. 3d. per barrel f.o.b.

£412	10	0
------	----	---

Total Gross weight. 80-12-1-13

Total Net. weight. 73-11-0-12

E. & O. E.



The advice and invoice having been received, it is the duty of one of the clerks to look out for the due arrival of the goods mentioned in the invoice, and also to attend to such other operations outside the counting-house as may be involved. In the meantime the invoice will be examined and prices compared with the order before payment of it is made.

**SHIPMENT OF GOODS.**—The next step in the exportation of the goods is the preparation of the Bill of Lading. This is, when signed, the actual representative of the goods. Bills of Lading are usually drawn in sets, the number in a set being at the option of the shipper. Generally, there are three, each bearing a sixpenny revenue stamp. The stamped Bills of Lading are signed by the master of the ship or by someone on his behalf. When signed, they are handed to the shipper of the goods, since they are his property. With each set of Bills of Lading, an unstamped copy, which is not for signature, is furnished to the shipbroker for the use of the master, and should be marked "Master's Copy." The *Bill of Lading* for the consignment of potatoes to Demerara is given as an inset. It will be seen that the particulars required in such a document are—

- (1) The name of the shipper.
- (2) The name of the ship.
- (3) The place of loading and destination of the ship.
- (4) A description of the goods shipped.
- (5) The place of delivery.
- (6) The persons to whom delivery is to be made.
- (7) The weight on which freight has to be paid.
- (8) The date.


If the shipper should choose to omit the name of the consignee on the face of the Bill of Lading, he may consign the goods "to order," in which case he must, before parting with it, endorse the document in order to make it available at the port of discharge. When a merchant is dispatching goods by the same vessel to several consignees, a separate Bill of Lading must be made out for *each* separate shipment.

Before preparing the Bill of Lading, it is always well to ascertain beforehand that the goods are sure of being dispatched by a certain ship. At times of pressure on a particular vessel, goods are often shut out for want of room. It is now the custom of important



steamship lines to require their shippers to use a special form of Bill of Lading, in which various stipulations as to what they will or will not be liable for are embodied. There are also special forms used for particular trades, the chief differences in which are the clauses at the end. The essential features of the document, however, are the same. The Bills of Lading, when made out, are taken to the office of the broker of the ship and left there in order that the signature of the master or his representative may be affixed. This is done after they have been examined to see that all the goods named on them are shipped. In due time, the shipper applies for their return and hands over in exchange for them the mate's receipts for any goods which have been loaded direct on to the ship from a barge instead of from the quay. The mate's receipt for the above-mentioned consignment to Demerara would be as follows—

#### 11. Mate's Receipt

Received on board the s.s. <i>Pergon</i> for DEMERARA	
	1,000 barrels Potatoes
Demerara	<i>ex</i> barge <i>Luna</i>
	(Signed) J. THOMAS, Mate.

The Bills of Lading are now in the possession of the shipper, and it becomes necessary to dispatch one or two of the set to the consignee (or to the banker as in this case), in order that he may be able to secure the goods on their arrival at the port of destination. One copy is sent as quickly as possible after the sailing of the ship, and another by a succeeding mail, the object being to secure the arrival of one out of the two, in case of loss or miscarriage of the other. The third part is retained by the shipper and kept with the other documents relating to the shipment.

With British shipowners, it is customary for them to secure, as far as they possibly can, all their freights at home; that is to say,












when their ships come from foreign ports the freight on the goods they bring is paid on the discharge of their cargoes, but when they go out to foreign ports, the freight is payable in advance. When this is the case, the shipbroker puts on each Bill of Lading the amount of freight payable for carriage of the goods named on it, and it is sometimes required that the freight must be paid before the Bills of Lading are given up. The following is the Freight Account of the consignment of potatoes to Demerara—

## 12. Freight Note

		LONDON, E.C.4.	
Messrs. GEO. PENNY & Co.			
<i>Dr. to Freight, etc., per s.s. Pergon, for DEMERARA.</i>			
 Demerara	1,000 barrels 80-12-1-13 at		
	25s. p. ton . . .	£100	15 5
	5% Landing Tax . . .	5	0 9
	25% War Surcharge on		
	£100 15s. 5d. . . .	25	3 10
		<hr/>	
		£131	0 0
		<hr/>	

It is the duty of Penny & Co. to see that the above account is correct before payment is made, and that the rates are those agreed upon. In this respect, it is well to remember that a ton of shipping varies somewhat, it usually being 40 cubic ft. in the case of goods which are bulky, whilst for heavy goods the ordinary ton of 20 cwt. is used.


Within six days of the clearance outward of the ship, the exporter is also required to deposit with the Customs Authorities a specification of the goods which he has exported. This will be entered by Penny & Co. on the form known in official language as the "Specification for British and Irish Goods only," a copy of which is shown on page 422. The particulars given on this form must be in accordance with the Customs export list, and



\* SPECIFICATION for British and Irish Goods only.

Port of London Ship's Name Bergon Master, James Abson for Demerara  
 Date of Final Clearance of Ship 26/4/19

\* The Specification of Goods exported must be delivered to the proper Officers of Customs within six days from the time of the final clearance of the Ship, as required by the Customs Laws.

Marks	Numbers	Description of Packages	Quantity and Description of British and Irish Goods in accordance with the requirements of the Official Export List	Weight		Value (l. s. d.)	Final Destination of the Goods
				Cwt.	lbs		
 Demerara	741	1000 Barrels	Potatoes	1471	12	£4.12 10 0	Demerara
				Total		£4.12 10 0	

! The "£ 0 0" or free on board value should be given

I declare that the particulars set forth above are correctly stated.

Signed George Perrygo  
 Date 26<sup>th</sup> April 19..  
 Address 165 Fenchurch Street  
 (Adding Exporter, or Agent, as the case may be)

Countersigned

Officer of Customs



have reference to the weight or measure and value of the goods. This information is used for statistical purposes; and to ensure its being given, the broker of every ship leaving any port in the British Isles is required under a penalty to deposit with the Customs within six days of the clearance outwards, a manifest which must contain full particulars of the whole of the cargo. If any goods shown in the manifest do not appear in the specifications, the Customs House authorities are able to apply to the shipper to remedy the omission. On the other hand, if goods appear in the specifications and not in the manifest, the broker can be called upon to explain. Repeated errors, through carelessness, are met with a small fine, but purely unavoidable mistakes are overlooked.

**EFFECTING INSURANCE.**—The goods having been shipped and the Bills of Lading secured, the exporter's remaining duty is to effect such insurance on them against sea risks as he may think fit. It is customary to insure exported goods for such an amount as will cover not only the value of the goods as shipped, but also a reasonable profit, and such a sum as would cover any expenses which would be incurred in the event of the loss of the goods or any part of them by perils of the sea. A reasonable profit is generally taken to mean 10 per cent., and about 2 per cent. is added for other charges named.

The insurance will be effected through the medium of an insurance broker, who receives his remuneration not from the merchant for whom he acts, but *from the underwriters*, in the form of a reduction of 10 per cent. on the premiums he arranges to pay. The following letter will, therefore, be addressed by Penny & Co. to the insurance broker asking him to quote a rate—

### 13. Asking for Insurance Quotation

FREDERIC BOLTON, Esq.,

Ocean Chambers, E.C.4.

Dear Sir,

Please quote us a rate for Marine and War Risk Insurance on a shipment of 1,000 barrels Potatoes, valued at £650, per s.s. *Pergon* from London to Demerara.

Yours faithfully,

GEORGE PENNY & Co.



The broker's quotation and its acceptance by Penny & Co. are contained in the following letters—

**14. Insurance Quotation given**

MESSRS. GEORGE PENNY & CO.,  
127 Walden Road, E.C.2.

Dear Sirs,

I thank you for your letter, and quote you 6s. 8d. % for Marine Risk (f.p.a.) and 20s. % for War Risk Insurance on the shipment named, and should be glad to learn if I may effect the Insurance.

Yours faithfully,

FREDERIC BOLTON.

**15. Accepting above Quotation**

FREDERIC BOLTON, ESQ.,  
Ocean Chambers, E.C.4.

Dear Sir,

We thank you for your letter. Please effect the Insurance at the rate quoted and send us Policy in due course.

Yours faithfully,

GEORGE PENNY & CO.

The method of procedure is for the broker to write on a slip the particulars of the insurance he desires to effect, and if it is intended by the owner of the goods to insure against total loss and general average loss only, he puts on the slip the letters "F.P.A.," which mean "Free of particular average," or, if the ship which carries the goods belongs to a nation which is then at war with any other nationality, the underwriters will demand that the insurance shall be "F.C.S.," or, "Free of capture and seizure," unless they are paid an extra premium to cover "war risk." When goods are insured "F.P.A.," the risk borne by the underwriter is considerably reduced, since he is not liable for any damage or injury to them, but only for total loss and general average loss, the owner of the goods taking any risk of damage. Having arranged his slip, the broker either writes on it the premium he is willing to pay or, without stipulating the premium, presents the slip to one of the underwriters with whom he usually does business.

**INVOICING THE GOODS.**—The shipment of the 1,000 barrels of potatoes having been completed, the next duty is to prepare the



*export invoice* relating to the transaction, which is a matter of no small importance. Where there are several items, all the invoices received from the different tradesmen at home must be got together with the various Railway and Dock Bills for carriage and wharfage relative to them, and all other accounts and documents

## 16. Merchant's Export Invoice

GEORGE PENNY & Co., LONDON.

Invoice of 1,000 barrels Potatoes shipped per s.s. *Pergon* from London to Demerara, for order, risk and account of Messrs. J. Edwards & Co., Demerara.

J.E.&Co. Demerara	1,000 Barrels Potatoes each 1½ cwt.				
	net (about) at per barrel f.o.b. 8s. 3d.	£412	10	0	
	Total net weight 73-11-0-12				
	FREIGHT—				
	80-12-1-13 at 25s. p. ton	£100	15	5	
	5% Landing Tax . . .	5	0	9	
	25% War surcharge on				
	£100 15s. 5d. . . .	25	3	10	
		£131	0	0	
	EXPENSES—				
	Bs/Lading, Postages and				
	Petties . . . . .	£0	5	6	
	Marine Insurance . . .	2	3	4	
	War Risk Insurance . .	6	10	0	
	Freight as per above. .	131	0	0	
			139	18	10
			552	8	10
	Commission 3% . . .		16	11	6
			£569	0	4

E. & O. E.

127 Walden Road, E.C.2.



concerning the goods, such as Freight Notes and Custom House agent's charges. In case there are several kinds of goods drawn from different sources, it is not necessary to detail the prices and quantities, but only to give particulars of marks and numbers, and against each separate parcel the name of the persons supplying the goods, with the amount of their account for them. Copies of the original invoices are usually attached, and these give to the receiver at their destination full particulars of prices, weight, measure, and other particulars it is necessary for him to know. After the whole of the tradesmen's accounts have first been set out, the amounts are added together, and the first, or net cost of the shipment is shown. In the export invoice shown there is only one item of purchases and, therefore, this constitutes the net cost of the shipment.

The charges or expenses, as Freight, Insurance, Bills of Lading, Dock Dues, and all other incidental expenses, are next grouped together. These, again, are totalled, and the sum of them is added to the cost of the goods. Finally, the sum of the net cost plus the expenses is added to the merchant's charge of commission for buying and shipping the merchandise dealt with in the invoice.

**DRAWING BILLS OF EXCHANGE AGAINST SHIPMENT.**—Being now complete, the invoice is next dispatched to the consignee of the goods in a letter similar to the following—

#### 17. Letter enclosing Invoice

Messrs. J. EDWARDS & Co.,  
Demerara.

Dear Sirs,

The present serves to enclose copy of Invoice for shipment of 1,000 barrels Potatoes per s.s. *Pergon* in execution of your esteemed order. For the amount—£569 0s. 4d.—we have drawn on you at sight, as per your instructions, instructing the Colonial Bank to deliver documents on payment.

We trust that this shipment will turn out to your entire satisfaction, and await your kind repeat orders as well as orders for any other class of goods in which you deal.

Assuring you of our best attention at all times, we are,

Yours faithfully,

GEORGE PENNY & Co.



SIGHT DRAFT

No. 1

2<sup>ND</sup> STAMP

April 26<sup>th</sup> 19. For £1000

Pay the First of Exchange  
to the Order

Second unpaid  
of The Colonial Bank

SOLD BY  
E. COX & SONS  
NEW COURT GATEWAY  
CHANCERY LANE  
LONDON W.C.  
ESTD 1825

Value, shipment of 1000 barrels which please to Account.  
potatoes 5<sup>th</sup> Bergen

To Messrs. J. Edwards & Co.  
George Penny & Co.  
Demerara.



At the same time, a letter is forwarded to the Colonial Bank by Penny & Co., asking them to collect the amount of the above-mentioned invoice. In accordance with the consignee's request, a sight draft is made out, and this, together with two Bills of Lading, copy of the invoice, and the insurance policy, are all sent to the banker in London. The latter, in turn, forwards them to his agent in Demerara, who does not part with them until the amount of the draft is paid. When this is done, the consignees, Messrs. J. Edwards & Co., are at liberty to take charge of the goods mentioned in the Bill of Lading.

#### 18. Instructing Banker to Collect against Documents

THE COLONIAL BANK,

E.C.2.

Dear Sirs,

We beg to hand you herewith our Sight Draft No. 7845 on Messrs. J. Edwards & Co., of Demerara, for *Five hundred and sixty-nine pounds and four pence* (£569 0s. 4d.), together with two Bills of Lading, Invoice, and Insurance Policy covering both Marine and War Risks.

Kindly collect this amount and deliver documents *on payment only* and remit us, in due course, a cheque for the exact amount of our draft, drawee paying all charges.

Yours faithfully,  
(Signed) GEORGE PENNY & Co.

#### TEST PAPER XXXVII

1. Mention the chief stages through which an export transaction has to pass in the course of its execution.
2. Explain the meaning of an Indent, and say what particulars are furnished by it.
3. On receipt of an Indent by a Commission Agent, what are his duties?
4. When goods are packed for export, how are the packages made easy of identification?
5. What information is contained in a Bill of Lading?
6. Explain the use of a Mate's Receipt.
7. Give a specimen of a Freight Note and state for what purpose it is used.
8. Explain the mode of procedure when effecting the insurance of goods intended for exportation.
9. You are an exporter of stationery and have received an order from Melbourne for your stock lines, value, say, £100. State the procedure you would follow in getting the goods to your customer in Melbourne.



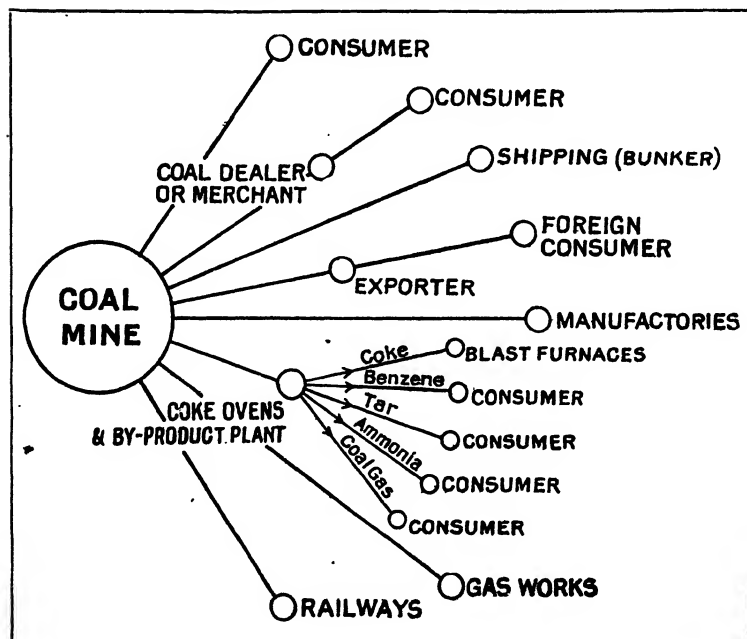
## CHAPTER XXXVIII

### TRANSACTIONS IN THE COAL EXPORT TRADE

GREAT BRITAIN is the most important country in the world for the export of coal. On the average the annual production of coal amounts to about 200 million tons, of which nearly one-fifth is exported abroad, this figure including the amount used in the shipping and bunkering trade. More than a quarter is also used by the three great industries: iron-making, gas-producing, and railways. A large amount of coal is also consumed in coke ovens and by-product plant. The chief by-products are ammonia, tar, coal gas, and benzene. The various channels through which coal reaches the consumer are shown in the diagram below.

**FUNCTIONS OF THE COAL EXPORTER.**—The coal exporter plays an indispensable part, not only in conducting, but also in developing,

### THE COAL TRADE.





by his initiative and enterprise, the coal export trade of the country. To this end he has built up at home and abroad an extensive and efficient organisation, well adapted to the needs of both producer and consumer. By means of this organisation, of which the exporters' intimate personal relations with foreign buyers are an inseparable element, he obtains orders and strives to maintain old markets while assiduously cultivating new ones. He is in no sense merely a broker drawing a commission between producer and consumer, as his relations with the collieries on the one hand, and the foreign buyers on the other, are totally dissimilar.

The exporter buys coal for export, as a principal, from the collieries for cash or on short credit terms, and consequently is responsible for payment of the coals before he himself receives payment from the foreign buyer, and even if he never does receive payment. Moreover, he buys for delivery at the loading port and even, in some districts, for delivery into wagons at the pit according to the varying requirements of individual collieries. Having bought the coal the exporter must issue the necessary shipping orders to, and must remain in constant touch with, the railway company and dock authorities until the coal is shipped, as he is responsible not only for the timely arrival of coal at the loading port, but also for the vessel engaged to carry the coal being loaded within the stipulated period of hours.

In selling abroad the exporter contracts on terms of delivery and payment which vary with the needs of the foreign buyer. Sometimes the coals are sold free on board at the British loading port (when the terms are known as f.o.b.); sometimes on terms known as c.i.f., which provide for the cost of the coal, dock dues, freight to the foreign port and insurance; and sometimes on "Delivery terms," by which the entire responsibility of carriage is borne by the exporter, either to the foreign port or to the foreign consumers' works in the interior. Thus it will be seen that a coal exporter must possess an extensive specialised knowledge of the home and foreign markets, trade conditions generally, railway and dock working, shipping freight markets, and above all, of the different qualities of coal, their physical and chemical properties and their uses.

**TRANSACTION IN THE COAL EXPORT TRADE.**—To illustrate the general procedure in the coal export trade, we shall now take an actual c.i.f. transaction. As a rule, such a transaction may be



grouped under four main headings, viz., the inquiry, the offer and acceptance, the shipment, and the payment.

**The Inquiry.** When an exporter or merchant receives an inquiry from abroad, before quoting he would first find the true financial position of his prospective client from a banker or inquiry agent.

**The Offer and Acceptance.** Should the "report" be a good one, he would then obtain a "firm offer" of the required parcel of coal, coke, or fuel either from the colliery salesman, or from a merchant who may have previously booked a quantity on speculation. The exporter would then estimate the amount of freight payable for tonnage, and the amount per ton for insurance and wharfage. His offer would then be telegraphed abroad. In the transaction below it has been presumed that the buyer is an Italian at Genoa, and should he accept this offer he would probably open a credit through a large Italian bank, instructing them to pay to the exporter £7,000 on presentation of the shipping documents, viz., the Bill of Lading, the Colliery Certificate, the Insurance Policy, and the *pro forma* Invoice. When credit has been opened in London, the bankers would advise the exporter, who would then accept the colliery company's or merchant's firm offer. This he would confirm by a Purchase Note, and in return a Sales Note would be received from the seller.

**The Shipment.** The exporter's next step would be to find a suitable steamer which could load in position with the Colliery "Stem." The original meaning of "stem" seems to be the same as that given to the word in such a phrase as "stemming a stream." Stemming means, therefore, the stopping or directing of a stream of coal coming down from the collieries in wagons to provide coal cargoes. The provision of stems is carried out between the shippers and the collieries, who, in turn, will make arrangements with the dock authorities for the necessary facilities. Thus, while the exporter arranges with the owner of a ship to charter his vessel, he will also arrange with the colliery to provide the stem. He will also instruct an insurance broker to effect insurance on the cargo.

**The Payment.** After the shipment of coal has been effected, the exporter would forward the necessary documents to his bankers, instructing them to collect the amount of the *pro forma* invoice from the Italian bank. For this service the banker may charge a fee of 2s. 6d. per mille.



**PROCEDURE IN THE COAL EXPORT TRADE.**—The actual procedure involved in the execution of a c.i.f. transaction would be as follows—

- (1) Request from the prospective buyer for quotations.
- (2) The written or telegraphic Offer.
- (3) The telegraphic or written Acceptance of the Offer.
- (4) The dispatch of the Purchase Note to the colliery company or merchant from whom the cargo is bought.
- (5) The receipt of the Sales Note from the colliery company.
- (6) The Charter Party.
- (7) The Stemming Note from the exporter to the colliery company.
- (8) The Insurance Policy.
- (9) Receipt of advice of credit having been opened by the customer's banker.
- (10) Notice of readiness from the shipowner or agent to the exporter, informing him that steamer is ready to load, and of the loading time as per charter party.
- (11) The Bill of Lading.
- (12) The Colliery Certificate stating that the coal has been shipped.
- (13) The "Sailing" Telegram to the importer.
- (14) Letter enclosing all necessary documents (required by the importer's bankers) to the exporter's bankers, requesting them to exchange for either cash, or guaranteed B/E (if arranged).

**Inquiry for Quotation.** A. Jones & Co. receive from C. Cortes the following—

#### INQUIRY FOR COAL

GENOA,

16th March, 19..

MESSRS. A. JONES & Co.,  
CARDIFF.

Dear Sirs,

I shall be glad to receive from you a c.i.f. price for 5,000 tons of Rhondda Merthyr Large Coal, to arrive here during April. Payment to be made by three months' Bill guaranteed by the Bank of Rome.

Kindly let me have your offer before the 28th instant.

Yours faithfully,

C. CORTES.



On receipt of this A. Jones & Co. would obtain a "firm offer" from the colliery company, or a merchant, holding Rhondda Merthyr Large Coal. Assuming that the price quoted them was 20s. per ton f.o.b. Cardiff, Penarth, or Barry, A. Jones & Co. would then estimate (or obtain offers from shipowners) the rate of freight they would have to pay, also the cost of insurance, and rate of discounting the B/E. The estimate would be summed up as follows—

	<i>s.</i>	<i>d.</i>
Coal . . .	20	—
Freight . . .	7	3
Insurance . . .		$\frac{1}{4}$
Discounting . . .		$2\frac{1}{4}$
Wharfage . . .		$3\frac{1}{4}$
Profit . . .		3
Total . . .	28	—

**Telegraphic Offer.** A. Jones & Co. would then telegraph C. Cortes—

#### QUOTATION

	<i>20th March, 19..</i>
C. CORTES.	
GENOA.	
Offer 5,000 tons 10% Rhondda Merthyr Large 28s. c.i.f. Genoa, shipment during April. Terms of payment as per yours 16th instant subject reply within seven days.	
	A. JONES & Co.

Assuming that C. Cortes telegraphs accepting this offer, he would instruct his bankers to hand over to A. Jones & Co. or their order, his B/E valued £7,000 on presentation of the following documents—

The Invoice.  
 Colliery Certificate.  
 Charter Party. (Copy if required.)  
 Insurance Policy.  
 Bill of Lading (stamped original).

The Bank of Rome would then instruct their London House, who in turn would inform A. Jones & Co.



## ADVICE OF CONFIRMED CREDIT

## BANK OF ROME

LONDON,

27th March, 19..

MESSRS. A. JONES & Co.,  
CARDIFF.

Dear Sirs,

*CONFIRMED CRÉDIT No. 4956, Account C. Cortes, Genoa.*

We beg to inform you that we have been instructed by our Genoa Branch to open credit in your favour, valid to the end of April, Seven thousand pounds (£7,000) about ninety days' sight against Invoice, Bill of Lading, Insurance Policy and Colliery Certificate, being the price of 5,000 tons (10% more or less) of "Rhondda Merthyr" Large Coal at 28s. c.i.f. Genoa.

Kindly let us know if this is in order.

We remain, Dear Sirs,

Yours faithfully,

BANK OF ROME.

N. POLLINI, *Manager.*

A Bill of Exchange would be drawn up by A. Jones & Co. and sent with a letter of acknowledgment to the Bank of Rome requesting them to have the payment ready when the necessary documents are presented.

**Purchase Note.** On receipt of the letter from the Bank of Rome A. Jones & Co. would immediately book the parcel of 5,000 tons "Rhondda Merthyr" Large Coal, and would confirm the order by means of a Purchase Note.



## PURCHASE NOTE

A. JONES &amp; CO.

COAL, COKE, &amp; FUEL EXPORTERS,

MERCHANTS, ETC.

TELEPHONE 1427.

Cardiff,.....28th Mar.,.....19.....

.....The Rhondda Merthyr Steam Coal Co., Ltd.,.....

.....Cardiff.....

Dear Sirs,

We beg to confirm the Purchase from you of about  
 .....Five thousand (5,000).....tons of.....Rhondda.....

Merthyr Large.....STEAM COAL for shipment at Cardiff  
 Penarth, Barry, or Alexandra Dock, Newport, Mon.,  
 for.....Cargo.....per S.S.....tonnage to be nominated  
 .....on or about.....prompt.....

Price.....Twenty shillings (20/-).....per ton f.o.b.

Terms Net Cash in 7 days or prompt Cash less  $\frac{1}{4}\%$ .

Buyer to pay usual Wharfage and Export Duty (if any).

In the event of riot, strike, lock-out, or stoppage of collieries, workmen or other hands connected with the working or delivery of the said coal, or in the event of accidents to mines or machinery, obstruction on the railway or in the docks or in the event of flood, frost, or storm, resulting in a stoppage, diminution of work at the collieries, or any circumstances over which Sellers have no personal control, they shall not be called upon to deliver coal during such stoppage or hindrance.

Yours faithfully,

A. JONES &amp; CO.



**Sales Note.** In exchange for this Purchase Note, Jones & Co. would receive a Sales Note from the seller or colliery company.

### SALES NOTE

RHONDDA MERTHYR STEAM COAL CO., LTD.

Cardiff,.....28th Mar.,.....19.....

.....Messrs. A. Jones & Co.,.....

.....Cardiff.....

Dear Sirs,

We beg to confirm the Sale to you of about.....*Five*  
*Thousand*.....(5,000).....tons of.....*Rhondda Merthyr Large*  
 STEAM COAL for Shipment at Cardiff, Penarth, Barry,  
 or Newport, for.....*Cargo*.....per S.S.....  
*tonnage to be stemmed*.....on or about.....*prompt*.....  
 Price.....*Twenty shillings (20/-)*.....per ton f.o.b.

Terms Net Cash in 7 days or prompt Cash less  $\frac{1}{4}\%$ .

Buyer to pay usual Wharfage and Export Duty (if any).

Mixing Charges, if any, to be paid by you.

In the event of riot, strike, lock-out, or stoppage of collieries, workmen, or other hands connected with the working or delivery of the said coal, or in the event of accidents to mines or machinery, obstruction on the railway or in the docks, or in the event of flood, frost, or storm, resulting in a stoppage, diminution of work at the collieries, or any circumstances over which Sellers have no personal control, they shall not be called upon to deliver coal during such stoppage or hindrance.

Yours faithfully,

RHONDDA MERTHYR STEAM COAL CO., LTD.

ROBERT SMITH,

*Director.*











**Tonnage Requirement List.** Jones & Co. would then endeavour to find "tonnage" to deliver this cargo and would probably affix to their office door a tonnage requirement list to inform the Chartering Clerks. The latter higgles or work the market each day, and call on various exporters.

TONNAGE REQUIREMENTS.

CPB/Genoa. 5,000 tons. ppt, 1,000, 6½d. try 7s.

This would indicate to shipowners that tonnage is wanted and that A. Jones & Co. would pay 7s. for a prompt vessel to load at Cardiff, Penarth, or Barry; also, that the rate of discharge at Genoa will be not less than 1,000 tons per day at a cost of 1s. per ton to the steamer.

Should the freight market rise, A. Jones & Co. would probably have to pay 7s. 6d. for a vessel to suit their requirements; should it fall they might obtain a lower price, say 6s. 9d. Any difference between their estimate and the actual price would be either a loss or a profit to them, as the case may be. Presuming they find a suitable steamer a Charter Party would be drawn up and signed by both parties, the original being left in the care of the shipowner.

C. Cortes would then be advised of the chartering of the vessel and the expected date of sailing to enable him to arrange for the discharging of the cargo on arrival of the steamer at Genoa.

**Stemming Note.** When the definite date of arrival and readiness to load of the s.s. *City* could be ascertained, A. Jones & Co. would hand to the Colliery Company a "Stemming Note," see page 438.

On receipt of this, the Colliery Company would arrange to have the coal at the agreed dock by the date of readiness, and Messrs. A. Jones & Co.'s coal foreman would also get in touch with the Colliery Company and obtain a "tipping order," which he would hand to the Dock Company, at the same time arranging a loading berth.



## STEMMING NOTE

CARDIFF,..... 28th March,.....19.....  
 .....*The Rhondda Merthyr Steam Coal Co., Ltd.*,.....  
 .....*Cardiff*.....

Dear Sirs,

Please Stem the.....s/s "*City*".....expected ready to  
 load at.....*Cardiff*.....about the.....30th inst.....for  
 about.....5,000.....tons of.....*Rhondda Merthyr Large*  
*Coal*.....on account of our.....*Sales Note dated to-day*.....

Time for loading.....180.....hours,.....from 30th  
 . March unless previously commenced.....

Yours truly,

For and on behalf of

A. JONES & CO.

A. LYONS.

When the vessel has sailed for the loading port, the sailing telegram is shown by the shipowner to A. Jones & Co., and definite docking orders would be given to her owners by them.

On arrival of steamer she would be ordered to commence loading, and a copy of the Charter Party would be handed to the Master by the owners.

**Notice of Readiness.** A "Notice of Readiness" would be served as follows—

## NOTICE OF READINESS

MESSRS. A. JONES & Co.,  
 CARDIFF.

Dear Sirs,

Please note that s.s. *City* is now (9 a.m.) in the Roath Dock, Cardiff, all ready to load as per Charter Party, and time counts accordingly unless previously commenced.

Yours faithfully,

B. WILSON & Co.



A. JONES & CO.

CARDIFF.

And at LONDON, SWANSEA,  
NEWPORT and HULL.

Colliery  
Railway  
Dock  
Works

weight. — Weight shipped unknown

CARGO

1,200 tons in No. 1 hold  
1,400 tons in No. 2 hold  
1,700 tons in No. 3 hold  
700 tons in No. 4 hold

Total 5,000 Tons

COALS ON BOARD FOR SHIP'S USE  
INDEPENDENT OF CARGO

tons in  
tons in  
330 tons in bunkers  
120 tons in bunkers on arrival

Total 450 Tons

SHIPPED at ..... CARDIFF ..... in good order and condition  
by A. JONES & CO. Steamship called the .....

of CARDIFF, in and upon the good ~~Motorship~~

"CITY"

whereof ..... R. EVANS ..... is Master for this present Voyage and  
bound for ..... GENOA

with liberty to sail without Pilots, and to call at any ports in any order, for bunkering or  
other purposes or to make trial trips after notice or adjust compasses all as part of the contract  
voyage.

Coal

Cargo of ~~Coal~~  
~~Patent~~ of ..... RHONDDA MERTHYR LARGE

... FIVE THOUSAND ..... tons } weight, weight shipped  
Railway }  
Colliery }  
Dock }  
Works }

unknown, which are to be delivered in the like good order and condi-  
tion at the said Port of ..... GENOA

unto ..... C. CORTES  
or ..... Assigns he or they paying Freight for the same as per  
Charter-Party dated ..... 28th March ..... 19 ..... all the terms,  
conditions and exceptions contained in which Charter-Party are  
herewith incorporated

General Average payable according to York-Antwerp Rules, 1924.

All the terms, provisions and conditions of the Carriage of Goods by Sea Act, 1924, and the  
Schedule thereto, are to apply to the Contract contained in this Bill of Lading, and the  
Owners and the Charterers are to be entitled to the benefit of all privileges, rights and  
immunities contained in such Act, and the Schedule thereto, as if the same were herein speci-  
fically set out, the unit under Article IV (5) being the ton. If, or to the extent that, any term  
of this Bill of Lading is repugnant to or inconsistent with anything in such Act or Schedule  
it shall be void.

IN WITNESS whereof the Master or Agent of the said Vessel hath signed  
..... One ..... Bill of Lading, all of this tenor and date drawn as a  
set consecutively numbered, any one of which being accomplished the  
others shall be void.

..... 4th April ..... 19 .....

For and on Behalf of the Master  
R. Stuart  
Agent.



It should be noted that in the Charter Party, A. Jones & Co. are allowed 180 running hours for loading, exclusive of time between noon Saturday and 6 a.m. Monday, also Bank Holidays, etc. Should the steamer occupy more time in loading, demurrage will have been incurred (with exception of strikes, lock-out clauses) at the rate of 6d. per gross register ton per running day, for which A. Jones & Co. will be called upon to pay.

**Bill of Lading.** When cargo has been shipped and the Dock Company's weights obtained, Bills of Lading are made out by the exporter, which the master or his agent signs.

It should be noted that in some trades "hours purposes" are stipulated on the Charter Party instead of time for loading and a minimum rate of discharge, e.g. "240 hours for loading and discharging." Where "hours purposes" are involved, in addition to demurrage, a "dispatch" clause is inserted. This signifies that should the steamer be loaded and discharged within the time allowed, the exporter can deduct from the Freight Account of the shipowner an agreed amount per gross register ton per running day, in lieu of the time unused.

**Sailing Telegram.** Immediately the s.s. *City* has completed loading the cargo and bunkers (coal for steamer's own use), by the terms of the Charter Party she is bound to proceed on the voyage.

When she has sailed, a "sailing" telegram is dispatched to C. Cortes—

#### ADVICE OF SAILING

C. CORTES,	4/4/19..
GENOA.	
Steamer <i>City</i> sailed 10 p.m.	
	A. JONES & Co.

The next step is for A. Jones & Co. to collect the B/E and to obtain an Invoice and a Certificate from the colliery that has shipped the coal. They would also declare insurance against their coal cover with the underwriters, adding 10 per cent to the free on board value to allow for the buyer's profit.



## COLLIERY CERTIFICATE

ALL QUOTATIONS, SALES AND CONTRACTS ARE SUBJECT  
TO THE USUAL STRIKE AND ACCIDENT CLAUSE

---

**The Rhondda Merthyr Steam Coal Co., Ltd.**

TELEPHONE: 6413 (TWO LINES)

CARDIFF.

TELEGRAMS:

"MERTHYR STEAM, CARDIFF"

*4th April, 19. .*

WE HEREBY CERTIFY that we have shipped per s.s.  
*City* at Cardiff Five Thousand Tons of Rhondda Merthyr  
Large Coal, and that same was fresh wrought at time of  
shipment.

5,000 Tons.

For and on behalf of

THE RHONDDA MERTHYR  
STEAM COAL CO., LTD.

ROBERT SMITH.



## COLLIERY INVOICE

*Shipping Ports—*

PORT TALBOT, SWANSEA,

CARDIFF.....*4th April, 19....*

NEWPORT, AND CARDIFF.

.....*Messrs. A. Jones & Co.,*..........*Cardiff*.....*Dr. to***The Rhondda Merthyr Steam Coal Co., Ltd.**

Date.	Particulars.	Truck No.	Weight. Tons.	At	£	s.	d.
<i>April 4</i>	<i>To Rhondda Merthyr LARGE Coal</i>		<i>5,000</i>	<i>20/-</i>	<i>5,000</i>	<i>-</i>	<i>-</i>
	<i>Shipped per s.s. "City" at Cardiff.</i>			.			
<i>E. &amp; O.E.</i>							



The following document is sent to C. Cortes in Genoa—

**CUSTOMER'S INVOICE**

CARDIFF..... 5th April,..... 19.....									
.....C. Cortes, Esq.,.....									
..... Genoa.....									
<i>In A/c with</i> <b>A. JONES &amp; Co.</b>									
19.. April 4	To Five Thousand Tons of Rhondda Merthyr LARGE Steam Coal, c.i.f. Genoa. @ 28/- per Ton		<table border="1"> <thead> <tr> <th>£</th> <th>s.</th> <th>d.</th> </tr> </thead> <tbody> <tr> <td>£7,000</td> <td>—</td> <td>—</td> </tr> </tbody> </table>	£	s.	d.	£7,000	—	—
£	s.	d.							
£7,000	—	—							
	per s.s. "City"								

Lloyds Bank would then proceed to collect the B/E and would hand it to A. Jones & Co.; or should Jones & Co. require ready cash, they would ask the bank to discount it for them.

**Payment of Freight.** The question of payment of freight next arises. After delivering the cargo to the consignees, the master or his agent would see that the Bill of Lading was endorsed, and would forward it to Wilson & Co., who would exchange it for the amount of freight due for the voyage.

With many c.i.f. sales, freight is paid at the port of delivery of the cargo, and when remitting to the exporter the importer deducts the amount required to cover the freight; but should the steamer require one-third advance of freight, notice is immediately given



to the importer, who takes the necessary steps to place the exporter in funds.

**Documents Sent to Bankers.** Should A. Jones & Co. have no reliable agent in London, they would write to their bankers enclosing the required documents as follows—

### BANKERS' INSTRUCTIONS

CARDIFF.

4th April, 19..

LLOYDS BANK, LTD.,

CARDIFF DOCKS.

Dear Sirs,

We beg to enclose herewith Invoice, Colliery Certificate, Insurance Policy, and Bill of Lading for cargo of Large Coal shipped per s.s. *City* now on passage to Genoa, cargo being consigned to C. Cortes, Genoa.

We shall be glad if you will obtain from the Bank of Rome, London, in exchange for the above documents their B/E value £7,000, which please discount at lowest rate, placing proceeds to the credit of our account with you.

Yours faithfully,

A. JONES & Co.

### TEST PAPER XXXVIII

1. On the average the annual production of coal in Great Britain amounts to about 200 millions tons. Trace briefly the channels through which this output is ultimately sold.

2. Draw the diagram on page 429 and explain its meaning.

3. Give a short account of the work of the coal exporter.

4. You are engaged in the coal export trade, and are shipping a consignment of coal to the Argentine. Explain the methods you would adopt (a) to secure an advance immediately the coals are shipped; (b) to make reasonably sure of payment from your customer.

5. The Egyptian Railway Company requires 30,000 tons of steam coal and 20,000 tons of patent fuel.

(a) Write a newspaper advertisement asking for prices and specifying time limit.

(b) Firm P. tenders for the above, giving prices, analysis, and details of shipment.

(c) Railway Company asks for a reduction of 1d. per ton on price of coal and ½d. per ton on patent fuel, respectively, and requests answer by wire.

(d) Telegram accepting reduction proposed.

(e) Sailing telegram of first consignment.

(f) Letter enclosing invoice and B/L and requesting future patronage.



## CHAPTER XXXIX

### ELIMINATION IN THE EXPORT TRADE

THE theoretical possibilities of including or excluding the middleman in the conduct of the export trade are illustrated by the diagram on page 446. All the members engaged in trade are shown on the diagonal of the diagram. These are—

- I. The Producer or Manufacturer.
- II. The Small Buyer.
- III. The Wholesale Buyer.
- IV. The Exporter.
- V. The Importer abroad.
- VI. The Wholesale Dealer engaged in the Import Trade.
- VII. The Wholesale Dealer engaged in the Home Trade of the Foreign Country.
- VIII. The Retailer abroad.
- IX. The Consumer.

**POSSIBILITIES OF ELIMINATION.**—If, therefore, a commodity is exported abroad and has to pass from the producer to the consumer in this unabbreviated way, it will become eight times the subject of a purchase and sale, since it passes through so many hands. The producer or manufacturer is confronted with the choice of eight different methods of disposing of his goods. On the other hand, each of the eight succeeding members has the opportunity of entering into connection with the manufacturer for the purpose of purchasing his finished goods. From the diagram it will be seen that—

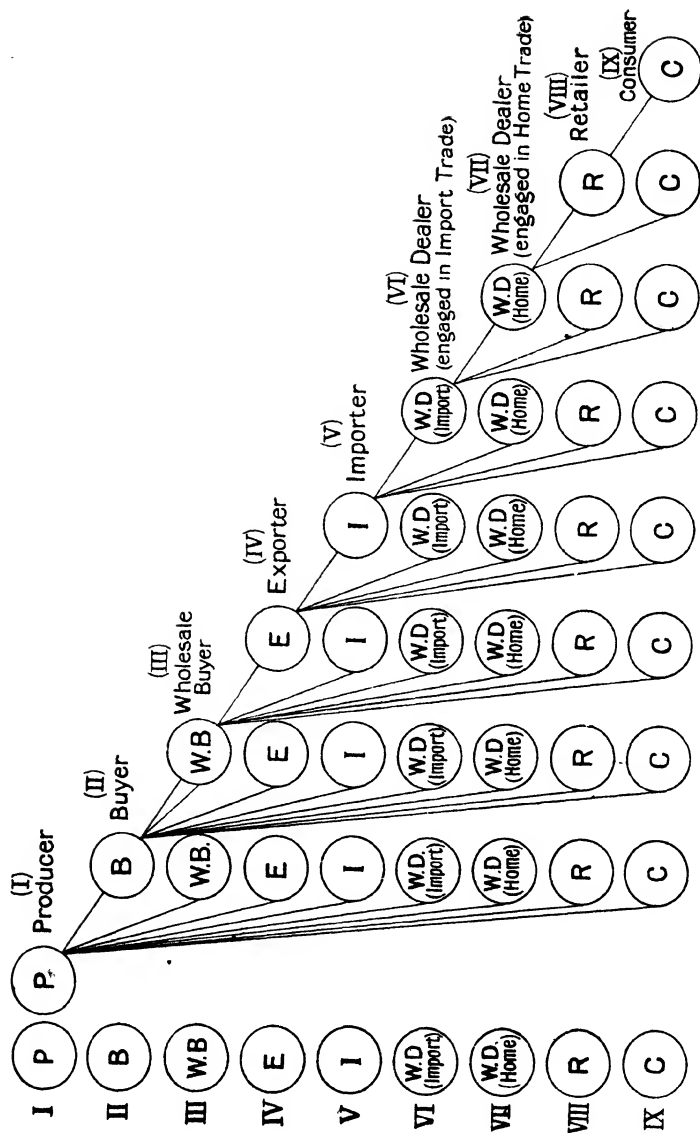
No. II (i.e., the Small Buyer) has only one method of effecting his purchase, but has seven different ways open to him for the execution of the sale, viz. Nos. III to IX.

No. III (i.e. the Wholesale Buyer) has two possibilities of making his purchase, and can choose from six different methods in the disposal of his goods abroad, viz. IV to IX.

Thus, it will be seen that each succeeding member engaged in the Export Trade has one possibility more for effecting the purchase, and one choice less than the preceding member for effecting



# ELIMINATION IN THE EXPORT TRADE





the sale. In this connection, it must not be overlooked that the initiative to eliminate a middleman may be taken by any of the intermediary members marked II to VIII, in the execution either of purchases or of sales. Every middleman plays both an active and a passive part in this process of inclusion and elimination. It is passive when a preceding or succeeding member considers it advantageous to renounce his services by undertaking the work himself. - Hence, it may be concluded that the existence of a middleman in the trading system depends upon the amount of useful and necessary service he can render in the distribution of the goods, which service cannot be performed so efficiently and economically by any other member of the community. This conclusion will generally be true so long as economic freedom is permitted to exist.

It is the duty of the trader to study this problem of elimination and to apply his knowledge to his own particular business. He should, in particular, discover to what extent this process of elimination has, in fact, been in operation, and should acquaint himself with the various possibilities of which he could avail himself in getting into touch with either the producer or consumer.

This would help to reveal to him the side from which the danger of elimination threatens him and the means at his disposal to meet these dangers. However, this is a problem of a specialised branch of the theory and practice of commerce, which every trader must try to solve for himself. It will be sufficient here to give a few of the more characteristic examples of elimination—

(1) **DIRECT TRADE BETWEEN PRODUCER AND CONSUMER.**—In this case, the whole of the middlemen marked II to VIII are eliminated. Examples are found in the sale of sewing machines and typewriters ; the supply of arms and munitions of war to the State ; the disposal of milk and dairy products through a central association established by the local farmers. In this direct intercourse with the consumer, the producer usually plays an active part, since he constitutes an integral part of the selling organisation.

(2) **DIRECT TRADE BETWEEN MANUFACTURER AND RETAILER.**—Here the manufacturer works hand in hand with the retailer, who may send his buyers into the districts of manufacture, or the manufacturer may sell his goods direct to the retailer. An example of the former is seen in the purchase of cotton goods



by native buyers. The latter, however, is the more common form of trade, and is exemplified in the sale of chocolates, boots, and clothing.

(3) **DIRECT BUYING AND SELLING BY THE EXPORTER.**—The wholesale merchant engaged in the export trade may eliminate all intervening middlemen by buying direct from the producer and selling direct to the consumer. The sale may be effected through retail stores or warehouses situated in the foreign country. The organisation of the export trade by the establishment of factories abroad, and the dispatch of one's own travellers to the selling area, are among the earliest forms of the export trade. Through the growth of civilisation, however, these forms of trade tend to disappear.

The fact that this form of direct sale to the foreign consumer is disappearing with the growth of civilisation in the area of consumption, and gives scope for more developed forms, may help to demonstrate that the tendency to increased division of labour, or the inclusion of further middlemen, is often more powerful than the opposite tendency of elimination. All the types of elimination which have hitherto been mentioned go to show that trade, as such, is not abolished, but is merely organised in a different form. For instance, the producer may link himself directly with the exporter by himself fulfilling the function of trade. In contradistinction to this form, there is one method of shortening the distributive process whereby trade itself is abolished (i.e. where the producer and consumer combine for their mutual good). This development has taken place in two directions—

(1) **The Establishment of Capitalistic Combinations.** The various stages of manufacture may be combined into a single undertaking, as in the case of mixed works, where coal-mining, smelting, the making of steel, etc., and other processes of manufacture are carried on. In this case, the coal, coke, and other minerals are utilised for the production of iron ore, which, in turn, is consumed in the manufacture of steel, from which are made all kinds of more highly finished articles. Thus, such an undertaking embraces the two functions of producer and consumer; and since there is no cessation of ownership during the transformation of the commodity, no trade takes place. Instead of the process of purchase and sale, there is a system of costing, the object of which is to determine the cost of



production of each stage, so that each succeeding stage may be charged with this amount.

Trade, with its characteristic feature of profit, emerges only when the last process of manufacture has been completed and the goods are sold to outside firms. The same principle is seen to operate in the textile industry, where combing, weaving, dyeing, spinning, finishing, etc., are often combined into a single business.

(2) **The Formation of Co-operative Undertakings.** A co-operative society of consumers may establish its own bakeries, dairies, slaughter-houses, boot and shoe factories; cultivate its own coffee and tea plantations; and possess its own ships for the transport of the goods. In this case, the operation of the trading function is restricted to the purchase of raw materials, whilst the finished product is distributed at cost price to the members.

In both the above forms, trade is abolished. Production is carried on for the consumers' own requirements.

**CHANGING CONDITIONS IN THE EXPORT TRADE.**—Since the War the conditions in the export trade have greatly changed. The exporter is now faced with impoverished populations in countries which retain a desire for British goods; with demands for credit, without any solid basis for granting it; and, in some cases, with organised foreign buying calculated to depress prices. He has to meet foreign competition, tariff barriers, and currency restrictions, and to compete with the modern range of alternative and inexpensive goods. In short, British goods have now to win their way where previously the road was clear. The individualistic theory of pre-War times with a ready sale for its product had no need to develop a marketing technique, and it now has no means of meeting adequately the economic difficulties of existing markets, or of opening up new markets.

The first essential for any readjustment of the export trade to modern conditions is to separate clearly the more permanent features from those which were appropriate to past development, but are no longer suitable. Encouragement, for example, should still be given to the pioneering spirit of the export merchant whose inheritance and experience have developed almost an extra sense for his calling. This, however, is not to say that the old type of individualism must continue. That type of individualism in present circumstances gives rise to a disorganisation which is patently



uneconomic, and constantly places the export merchant at the mercy of adverse market conditions. While the single firm can well remain in some ways the unit for enterprise, the pioneering spirit cannot hope to have a fair chance unless backed by *collective action*, not only in trading operations, but also in relation to finance and transport.

Similarly, there are many new problems in marketing which the exporter cannot hope to meet without organisation. In present circumstances, where the instinct of necessity is for each to scramble individually for the business, there are bound to be weak sellers, and concentration of effort to secure economy in costs, or to organise a drive on selective points by a central marketing agency, is impracticable. In every direction, therefore, the problems of the export trade call for organised action.

**NEW APPROACH TO EXPORT MARKETS.**—The need for strong and cohesive organisation so as to withstand the disintegrating influences at work in the existing export trade is apparent. Since much of the export field now falls within the sphere of reciprocal arrangements between governments, there must be an authority, representative of the particular branch of export trade, that can present its case to the Government, and also an organisation which can follow up the market when it has been opened to it. In so far as it meets with organised and powerful buying agencies, it must do so with equal strength.

Such an *export organisation* should be conceived not merely as a defensive counter weapon, for, in the long run, its chief advantage would be as a constructive instrument necessary in the search for new markets. Of course, organisation cannot by itself be a guarantee that lost markets will be recovered or new markets won. But once the export trade is properly equipped with the right type of organisation, it will, at any rate, possess the most effective instrument for essaying this task.

### TEST PAPER XXXIX

1. Copy the diagram on page 446 and explain its meaning.
2. How many possibilities has the export merchant of making his purchases, and what different methods are open to him of disposing of his goods?
3. Give illustrations of the sale of commodities in which all the middlemen are eliminated.
4. State three cases in which the manufacturer distributes his goods directly through the retailer.



## CHAPTER XL

### FURTHER DOCUMENTS USED IN TRADE

IN the present chapter the following documents which are used in trade will be explained—

- |                           |                            |
|---------------------------|----------------------------|
| 1. Export Invoices        | 5. Account Current         |
| 2. Consular Invoices      | 6. Documentary Bill        |
| 3. Certificates of Origin | 7. Letter of Hypothecation |
| 4. Account Sales          |                            |

**EXPORT INVOICES.**—When the commission agent purchases goods for the account of a house abroad, he prepares an account containing the price of the goods, and to this he adds the cost of transport, insurance, commission, and any other expenses. The practice has arisen for the customer abroad to ask for a price which includes all these expenses. The commission agent, who receives an indent from abroad for various kinds of goods, endeavours to get the best terms from the manufacturers, and then charges an inclusive price to his client, containing all the expenses together with a profit. There are, however, various methods of quoting prices in foreign trade, the chief of which may be shown as follows—

#### ELEMENTS INCLUDED IN PRICE

1. Manufacturer's Price	L	Free	F.	F.	C.	C.	F
	o	on	A.	O.	B.	I.	R
	e	Wag-	S.	F.	F.	F.	A
	o	on.					N
2. Carriage to Station.							C
3. Dock Charges . . . . .							O.
4. Loading Charges . . . . .							
5. Export Duty . . . . .							
6. Freight . . . . .							
7. Insurance . . . . .							
8. Landing Charges in Foreign Country. . . . .							
9. Transport Charges to and by Station . . . . .							
10. Local Delivery Charges . . . . .							
11. Commissions. . . . .							

“Loco.” A “loco” price gives the cost of the goods at the



place of purchase. This mode of quotation is very rare. The seller or manufacturer undertakes to keep the goods in his warehouse at the disposal of the buyer, who is responsible for all the expenses of removing the goods to their final destination. Hence the price quoted is sometimes referred to as "*ex* warehouse" terms.

**Free on Wagon.** This price leaves the seller of the goods responsible for all the expenses incurred in placing them on the wagon at a stated place.

**Free Alongside Ship.** A quotation containing a stipulation of this nature requires the goods to be delivered alongside the ship or wharf at the seller's expense. In such cases, the risk is the seller's until delivery has been made as stipulated.


**Free on Board.** The invoice price of goods so sold includes the expense of delivery on board ship. The risk is the seller's until delivery, after which the buyer assumes liability both for insurance and for freight.

**Cost and Freight.** This price includes all charges up to the destination of the vessel, except insurance.

**Cost, Insurance, and Freight.** This phrase denotes that the price quoted will cover the cost of the goods and also the expenses of insurance and carriage.

**Franco.** This is sometimes referred to as "franco domicile," "rendu," or "free." When goods are quoted on these terms, the price includes all charges up to and including delivery at the buyer's address. This includes any import duty, carrier's charges, and every other possible charge.

It is usual to make out at least three copies of an export invoice and, although the forms vary to a considerable extent, the particulars usually included are shown on the following invoices—

**Loco INVOICE.**—Suppose a "loco" invoice has to be prepared for the following particulars of goods shipped by Hollingworth & Co., of Manchester, to Messrs. Fonzes & Co., Marseilles, per s.s. *Swift*, from Goole, in 10 cases marked  Nos. 41/50—

30 pcs. 26" Black Novelties, 60/62 yds., the lengths being 2/61, 8/62, 7/61½, 7/61½, 6/63 at 8½d. per yard. The charges for packing were 6s. 6d. per case; carriage to Goole 15s., and freight to Marseilles at 18s. 9d. per ton and 10 per cent., each case measuring 2' 10" × 1' 9" × 1' 11"; B/L and Shipping Charges, 16s. 8d.; Marine Insurance (for 10 per cent. above invoice value)



at 4s. 6d. per cent. and stamp. This would be made out as follows—

### LOCO INVOICE

<p style="text-align: center;">INVOICE OF TEN CASES NOVELTIES</p> <p style="text-align: center;">shipped by the undersigned per s.s. <i>Swift</i>,</p> <p style="text-align: center;">Goole to Marseilles,</p> <p style="text-align: center;">by order and for account and risk of</p> <p style="text-align: center;">MESSRS. R. FONZES &amp; CIE, MARSEILLES.</p>									
30	<div style="border: 1px solid black; padding: 2px; display: inline-block;">F. &amp; Co., Marseilles</div>	41/50							
			£	s.	d.	£	s.	d.	
	<p><i>pcs. Black Novelties—</i></p> <p>60/62 yds., 2/61, 8/62,</p> <p>7/61½, 7/61½, 6/63 =</p> <p>1,858½ yds.</p>	<i>d.</i>				67	15	4	
	<b>Charges—</b>								
	10 Cases, ----- per case .	6/6	3	5	—				
	<i>Railway Carriage.</i>			15	—				
	<i>Freight on 95' 0", 18/9 + 10%</i>		2	9	—				
	<i>Shipping Charges</i>			16	8				
	<i>Marine Insurance on £80 .</i>			3	10	7	9	6	
	<i>E. &amp; O. E.,</i>					£	75	4	10
	<i>Manchester, 7th Aug., 19 -</i>								
	<i>John Hollingworth &amp; Co.</i>								

F.O.B. INVOICE. If the goods mentioned in the above "Loco" Invoice were quoted at F.O.B. terms, the invoice would be made out as follows.

	£	s.	d.
Cost of Goods . . . . .	67	15	4
Cases . . . . .	3	5	—
Shipping Charges . . . . .	16	8	
Railway Carriage . . . . .	15	—	
	<hr/>		
	£72	12	0



Since there are  $1,858\frac{3}{4}$  yds., the price per yard would be—

$$\frac{\text{£}72\ 12\ 0}{1,858\frac{3}{4}} = 9\frac{3}{4}\text{d.}$$

per yd. f.o.b.

The invoice would then appear as follows—

### F.O.B. INVOICE

#### INVOICE OF TEN CASES NOVELTIES

shipped by the undersigned per s.s. *Swift*,

Goole to Marseilles,

by order and for account and risk of

MESSRS. R. FONZES & CIE, MARSEILLES.

<div style="border: 1px solid black; padding: 2px; display: inline-block;">F. &amp; Co., Marseilles</div>		41/50						
30	pcs. Black Novelties—		£	s.	d.	£	s.	d.
	60/62 yds., 2/61, 8/62							
	7/61½, 7/61½, 6/63 =	d.						
	1,858½ yds.	9½				72	12	—
<b>Charges—</b>								
Freight on 95' 0", 18/9 × 10%			2	9	—			
Marine Insurance on £80 .				3	10	2	12	10
Manchester, 7th Aug., 19—								
John Hollingworth & Co.						£	75	4 10

**C.I.F. INVOICE.** If a c.i.f. quotation were required, the gross amount of the last invoice would be divided by the number of yards, in order to quote a price per yard which would include all charges up to the port of delivery. The invoice would then contain one item only—

30 pcs. Black Novelties—

60/62 yds., 2/61, 8/62

7/61½, 7/61½, 6/63 = 1,858½ yds. @ 9½½d.

= £75 5s. 3d.

**FRANCO INVOICE.** If a "Franco" quotation were given, the



measurements and money would be made out in the foreign equivalent. For example, the goods mentioned in the above invoice would be charged in metres instead of yards; and to the total c.i.f. price would be added the export or import duties, the forwarding charges from the port of arrival to the buyer's premises. When these have been calculated, the sum total is divided by the number of metres to arrive at the cost per metre.

The following is a specimen Franco Invoice—

### FRANCO INVOICE


BRADFORD;

12th October, 19\_\_.

Messrs. BERTET, RENAUDIE & CIE, ROUBAIX.

*Dr. to* ALEXANDER, MUNN & Co.

Sent for your account and risk to *The Goole Steam Shipping Co., Goole,* for Shipment per next steamer to Messrs. *Jules Petit & fils, Boulogne.*

1	Bale			
		ROUBAIX		
60	Bdls. 2/12 Coating	(600 lbs.)		
		Kilos 272.15 @ Fcs. 4.60		1251.90
		Discount 3 %		37.55
				<u>1214.35</u>
		Franco domicile		
		Roubaix.		
		Due 30th November, 19__		

**CONSULAR INVOICES.**—Certain countries, notably the United States and most of the Republics of South America, require that goods exported to them shall be accompanied by an invoice describing the quantity, quality, and the nature of the goods, in order that the Customs duties should not be evaded. (A Consular Invoice for Hayti is shown as an inset.) These invoices are signed by the Consul of the country to which the goods are being



shipped. The usual method is to take to the Consul for signature the necessary number of invoices signed by the head of the exporting firm ; and when these are certified by the Consul, a copy each is given to—

- (1) the shipper ;
- (2) the Customs Authorities at the port of entry ;
- (3) the Consul.

For some countries, these invoices are made out in English ; but often they are required in Spanish.

A fee of varying amount is charged by the Consul for certifying these invoices. Since they are necessary for the clearing of the goods abroad, the particulars given must be very accurate, as a great deal of trouble, and even loss, is occasioned if the particulars given are not in strict accordance with the requirements of the importing country.

**CERTIFICATES OF ORIGIN.**—This is a document declaring the place of origin of goods for exportation, and states where they have been grown or manufactured. These certificates of origin have to be prepared by the exporter in order to secure preferential duties when dispatching goods to Italy, Spain, South Africa, Australia, and Canada. The forms are sometimes printed on the back of an ordinary invoice, or they may be obtained from the local Chamber of Commerce ; or from the Custom House at the time the goods are entered. They must be signed by exporter or his agent, or by the Secretary of the local Chamber of Commerce. (A facsimile Certificate of Origin is shown on page 457.)

Since duty is charged on the net amount of the invoice, care should be taken to deduct all trade and cash discounts ; and the whole of the invoice must be made out either in the same handwriting or in the same typewriting, otherwise the Customs will not pass it.

**ACCOUNT SALES.**—This is the name given to the document sent by the commission agent or broker to his principal for whose account the goods have been sold. It shows—

1. The weight, gauge, measure, etc., of the goods sold.
2. The price obtained per unit, and the total price, or gross proceeds.
3. Any expenses, such as freight, dock charges, insurance, etc., paid by the agent.







# CONSULAR INVOICE

No. 39

Consular Invoice of 5 Packages Shipped per "Bulie" Gross tonnage --- Captain J. Jones  
of Liverpool by Messrs. Richard Bulman & Co. of Liverpool  
to Port-au-Prince Hayti Consigned to Messrs. Leon Dreyfus & Co.

Mark and Counter Mark	Numbers	No. of Packages	Description of Contents	Width in Inches	No. of Yards	Pieces or Dozens	Value £                      s.                      d.		
G D & C S Port-au-Prince "	60/63	4	Checks	22 1/23	23,912	1000 pieces	171	4	11
	64	1	Morlaix de Coton	33/34	5,994	999 pieces	55	3	1
		5					£226	8	0
CHARGES									
FREIGHT									

**TOTAL GROSS WEIGHT.**

We sincerely declare that this invoice is in perfect accordance with the truth and agrees in every respect with our books, and that neither the precise designation, nor the weights, quality, quantity, nor value of the goods stated herein have been altered.

Liverpool, 10th December, 19--







## CERTIFICATE OF ORIGIN.

I, *Wm. John Jeffery*, hereby certify that I am *Chief Clerk* of Sir Isaac Pitman and Sons, Ltd., the manufacturer(s) of the articles included in this invoice, and that supplier(s) I am duly authorized to make and sign this certificate on behalf of the said manufacturer(s) supplier(s) Sir Isaac Pitman and Sons, Ltd.

I have the means of knowing and I do hereby certify that this invoice from the said Sir Isaac Pitman and Sons, Ltd., to *Messrs. F. Heywood & Co., Cape Town*, amounting to *Twelve Pounds, Sixteen shillings* is true and correct, and that all the articles included in the said invoice are bona fide the growth, produce, or manufacture of the United Kingdom, and that a substantial portion of the labour of that country has entered into the production of every manufactured article included in the said invoice to the extent in each article of not less than one-fourth of the value of every such article in its present condition, ready for export to South Africa.

*Wm. John Jeffery.*

Dated *London* this *30th* day of *September*, 19..







not only in amount, but in incidence, it is usual to pay and allow interest on each item brought in, from the date on which it appears to that on which the account is closed. An Account Current enables the firm receiving it to ascertain the exact state of affairs between them and their friends in another part of the world.

*Example—*

Wm. L. Curtis & Co., London, sell goods to J. Fuller, of Calcutta, as follows—

7th August, £348 ; 18th August, £291 ; 10th December, £375. Remittances are received for £375 due 10th September, and for £400 due 29th November. Interest is allowed *pro* and *con* at 5 per cent. per annum, and the balance at 31st December is to be shown. The interest items are: £6 19s. 5d., £5 7s. 7d., £1 1s. 7d. £5 15s. 9d. ; and £1 13s. 4d.

The Account Current would appear as shown on the next page.

**DOCUMENTARY BILL.**—This is a bill of exchange which is accompanied by documents, such as a bill of lading, a dock warrant, a delivery order, a policy of insurance, and an invoice. It is drawn in payment of goods shipped to a foreign country. The consignee to whom the goods are exported cannot obtain possession of them without producing the bill of lading. In order to procure it, he must accept the draft attached to it, that is, he must sign it to undertake that he will pay the amount in a certain time. The usual procedure is for a merchant, say, in London, shipping goods to a firm in Calcutta, to send the bill of exchange and bill of lading to a bank or to an agent of his there, with instructions not to give up the bill of lading to the purchaser unless he accepts the bill of exchange, which is then either returned to London or converted into cash at Calcutta. In case the purchaser should decline to accept the draft, he is not allowed to take the bill of lading ; and then the agent of the seller claims the goods, since they will be delivered to him on presenting the bill of lading to the vessel's agents.

**LETTER OF HYPOTHECATION.**—Where a banker makes a loan to a shipper on documentary bills of goods consigned to a client abroad, he sometimes requires a "Letter of Hypothecation" or a "Letter of Lien." The former is the more usual, and empowers the collecting bank to sell the goods in the event of the bill being dishonoured. When an exporter is constantly obtaining advances



**LONDON.**

31st Dec., 19--

Mr. J. Fuller,

## IN ACCOUNT CURRENT WITH

Dr.

**WM. LUCIUS CURTIS & CO.**

Cy.

[illegible]



from the bank, he often signs a "General Letter of Hypothecation," which has reference to all future transactions.

The following is a form referring to a particular shipment—

### LETTER OF HYPOTHECATION

MANCHESTER.

12th July, 19\_\_.

To the Directors of the      *Blankshire Bank, Ltd.*  
· *London.*

GENTLEMEN,

We send herewith      30 days' sight bill drawn by  
*ourselves* on *Messrs. Jones & Co., Bombay*, for  
£600, and, as security, forward with the said bill,  
shipping documents for the following goods—

*Invoice for 10 bales Prints valued at £600.*  
*Policy of Insurance F.P.A. for £700 payable in Bombay.*  
*Bill of Lading for 10 bales Prints marked C. & Co.,*  
*Bombay, 1/10 per s.s. "City of York": from Birken-*  
*head to Bombay, the freight on which, amount-*  
*ing to £6 5s., is paid by ourselves.*

These documents are to be given up on payment of  
the bill.

If the said bill should suffer dishonour, we hereby  
authorise you to cause the said goods to be sold, such  
sale being for our account, at our risk, and subject to  
the usual charges for commission and all incidental  
expenses.

Against the above, please advance      90%,      viz.,  
£540,      as arranged.

Yours faithfully,

THOMAS BROWN & Co., LTD.



## TEST PAPER XL

1. Explain the terms "loco," F.O.B., C.I.F., and Franco, in connection with the price of goods.

2. A merchant may quote a price for goods F.A.S., which means that the price includes the cost of conveying the goods to the ship's side. Mention five other kinds of prices commonly quoted for goods, give their commercial abbreviations, and explain exactly what the prices mean.

3. Taking a "loco" price as a basis, name what additions would be required to make this into—

(a) a C.I.F. price

(b) a Franco price.

4. Make out an Export Invoice ("loco") for the following goods, sold by Lucius Curtis & Co., Manchester, to Monsieur Fonzes, Marseilles—

8 cases, 45 pcs. each, 34" White Shirtings (Pat. No. 326) at 6s. 6d. per piece. Packing, 6s. per case. Carriage to London and Freight (through rate) at 22s. per steamer ton and 10% primage. Each case measures 3' 2" x 2' 4" x 1' 11". Marine Insurance F.P.A.\* 3s. 6d. % for 10% over invoice value) and stp. B/L and charges, 4s. 9d. Shipped from London per s.s. *Marsala*.

5. Make out a Franco Invoice from the particulars given in Question 4. Import duty, Francs, 350; Exchange, 124.3.

6. From the particulars given below, make out a Franco Invoice—

*Shippers*: B. Burton & Co., Manchester.

*Buyers*: J. George & Co., Amiens.

Shipped by s.s. *Swansail* from Hull.

5 c/s (containing 150 pieces) black Jeannettes, 9,800 yards at 7d. per yard.

*Note*. One yard = M. 0.9144. £1 = Fcs. 124.2.

The measurement in the above invoice must be given in metres, and the price charged in French currency.

7. What is a Consular Invoice, and what purpose does it serve?

8. What is a Certificate of Origin, and for what purposes are such documents used?

9. Make out an Account Sales of 50 barrels Coffee *ex* "Swift" from Kingston, Jamaica; sold by Roger Gray & Co., Liverpool, on account of Messrs. John Fuller & Co., Kingston. Gross weight, 96 cwt. 2 qrs. 8 lbs.; tare, 9 cwt. 2 qrs. 12 lbs.; draft, 2 cwt. 1 qr. 8 lbs. Sold at 68s. per cwt.

*Charges*: Entry, Dock and Town Dues, 13s.; Marine Insurance on £350 at 10s. % and stp.; Freight on 96 cwt. 2 qrs. 8 lbs. at 47s. 6d. per ton of 20 cwt.; Cartage and Portage, £1 3s. 6d.; Consolidated Rate, £4 17s. 3d.; Fire Insurance, 6s.; Auction Expenses, 8s. 4d.; Bank Commission and Interest on Charges, 9s.; Commission and *del credere* at 2½%.

10. Explain what is meant by an "Account Current," and make out such an account for Alfred Bridger in respect of the following transaction with Harry Curtis—

19—

Jan. 17. Goods sold to Harry Curtis, £200, due 1st February.

Feb. 1. Received cash from Harry Curtis, £50.

Mar. 18. Goods bought of Harry Curtis, £300, due 1st April.

Apr. 1. Paid to Harry Curtis, cash £200.

May 1. Goods bought of Harry Curtis, £150.

" 10. Goods sold to Harry Curtis, £120, due 1st June.

The account to be made up to 1st June, 19—; interest to be at 6 per cent. per annum, which may be calculated by months instead of days.

11. "Bill of Exchange with shipping documents attached." What are these shipping documents? Describe the functions of each, and explain why the documents should be attached to a Bill of Exchange.

12. What is meant by a Letter of Hypothecation?



## CHAPTER XLI

### INSTITUTIONS FOR THE FURTHERANCE OF TRADE

THE heading "Institutions for the Furtherance of Trade" is understood to embrace all those arrangements by which, directly or indirectly, trade is facilitated.

The chief institutions through which trade is directly furthered are Markets, Fairs, and Exchanges, etc.; whilst those through which it is only indirectly influenced are Chambers of Commerce, Trade Organisations, etc. There is, of course, a whole series of such institutions, but only the most important of them will be considered in this chapter.

**MARKETING INSTITUTIONS.**—Wherever exchange, i.e. the purchase or sale of goods, has become a permanent necessity, buyers and sellers meet together at certain times and places to equate demand and supply, and markets evolve as permanent institutions. Organised market places have been used for centuries to aid in the distribution of merchandise, and the markets and fairs of the Middle Ages were an important part of the market structure of that time. Originally, all produce markets served for the direct exchange of commodities between producer and consumer and were, in essence, retail markets. With the development of commercial agriculture, many farmers marketed a greater volume of produce than they could conveniently sell in small lots to consumers; similarly, particularly in areas where production tended towards specialisation, a considerable quantity of produce was raised which was surplus to local demand and had to be marketed further afield. The first gave rise to the local trader who specialised in retail distribution; the second to the country dealer who specialised in the collection and assembling of produce for dispatch in bulk to distant consuming centres. In some instances, country markets have reacted to these developments by changing gradually from retail to mainly or wholly wholesale trade. At the present day, the following types of organised markets may be distinguished—

(1) **Retail Markets.** These markets, dealing mainly in foodstuffs, are mostly held on sites which have been used for generations



They vary from small open-air "farmers' markets" held weekly or bi-weekly in market squares in country districts, to the daily markets held in commodious halls in large cities. Both classes of retail markets—open and covered—are tending more and more to change from centres mainly for the sale of foodstuffs to mere arcades of stalls for the sale of haberdashery, crockery, books, clothing, ironmongery, and toys. The argument in favour of admission into the market of a variety of trades is that the market is thus made attractive to all classes of the community and costs are spread. Street or kerb markets are found in large towns and cities. The existence of a flourishing street market is probably evidence that a municipal retail market would succeed in the neighbourhood. For traffic reasons, street markets are now in process of disappearing from main thoroughfares.

(2) **Fairs.** The chief difference between a market and a fair lies in the fact that fairs are, as a rule, bigger, and are not held so frequently as markets which deal largely with perishable foodstuffs. They are generally held on a fixed day or days in the year—in many cases a saint's day. Fairs play a relatively small part in present-day marketing in England, and have survived chiefly as pleasure fairs. Exceptions to this statement are of comparatively recent development, such as the British Industries Fair, the Radio Exhibition, and the Motor Show. From the seller's point of view, the value of such fairs as these is incalculable. Without incurring the cost of carriage and the risk of transporting valuable goods, he can present to his prospective customers actual samples of his goods and discuss terms with them face to face. The buyer, on his side, can see at one visit all that the manufacturers have to offer; can compare prices and enter into direct relations with principals; and by exchanging experience with them, can form a fairly accurate judgment as to the direction of public taste.

(3) **Auctions.** The most outstanding characteristic of the auction is that it is usually open to the public, and that goods are sold to the highest bidders. Any person who wishes to do so is free to attend and make purchases, provided that he complies with the rules under which the sale is conducted. When properly conducted, therefore, it would seem that the auction is one of the fairest methods of selling goods, though it is frequently alleged that a considerable amount of manipulation goes on both on the part of the vendors



of the goods and amongst combinations of buyers. Although the majority of auctions are open to all buyers, in certain instances this is not the case. In the fruit trade, for example, the question of the closed saleroom has long been the subject of controversy. At Liverpool there exists an agreement between brokers and members of the Buyers' Association to keep the saleroom to themselves. New members are elected, but only in small numbers, and are required to pay a substantial entrance fee. The auction provides a quick way of disposing of large quantities of such raw materials as furs, wool, some agricultural produce, and, more rarely, manufactured goods.

(4) **Specialised Wholesale Markets.** These markets, which are mainly concerned with agricultural produce, are generally found in towns of 100,000 or more inhabitants, and with very few exceptions are owned by local authorities. They are a great convenience to the retail trade in that they enable the quality and price of large supplies of a wide range of commodities to be quickly compared, and a selection made to the best advantage. They help to steady prices; they also help to ensure that prices are a reasonably fair reflection of the relation of supply and demand. Further, the concentration of produce at wholesale markets facilitates food inspection and other public health services, and makes for speedy and economical distribution. Finally, a recognised wholesale market, the tenants of which may mostly be old-established firms, should give confidence to distant suppliers. If these functions are to be discharged effectively, it is essential that the markets should have ample accommodation for something more than normal supplies. They should, for instance, be able to provide to a reasonable extent for the seasonal variations in the supplies of fruit and vegetables and fish, and for unusual increases in the supply. Unless accommodation is provided to this extent the producer and the consumer may be penalised, the former because he is unable to find an immediate market for his produce, which by reason of its nature in many cases will not keep, and the latter because he is deprived of the benefit which might otherwise accrue in respect of lower prices resulting from supplies above the normal.

(5) **Produce Exchanges.** A produce exchange is an organisation of dealers in certain commodities, which provides a market place where the members meet at definite times and transact business under the



rules laid down by the organisation. In addition to providing a trading place and regulating the business dealings of its members, a produce exchange generally provides a method for settling trade disputes, establishes uniform grades for the commodities dealt in, and gathers and distributes market information. The exchange itself has no dealings in the commodities handled by its members. Its function is simply to provide facilities for the transaction of business, and to regulate the business dealings of its members. Before a commodity can be the subject of dealings on an organised produce exchange, five conditions must be satisfied, namely—

(a) It must be possible to hold stocks of goods at convenient points.

(b) The commodity should be capable of being numbered, weighed, or measured.

(c) The quality or grade should be capable of being tested easily.

(d) The dealings in the commodity should be frequent.

(e) Prices should be subject to fluctuation.

The commodities dealt in on these exchanges are of such a kind that they can be bought without being seen. In other words, they must be capable of being *graded*. It is also necessary that they should be capable of substitution, so that it is immaterial what particular lot a buyer receives. The produce exchanges are of two types: *general exchanges* where a number of commodities are dealt in, such as the Commercial Salerooms or the Baltic Exchange, and *special exchanges* where one commodity only is the subject of dealing as in the case of the Wool Exchange in London, or the Liverpool Cotton Exchange.

**THE CORN EXCHANGES.**—England is the most important wheat and flour importing country in the world. The chief centres for this trade are London, Liverpool, Hull, Southampton, Manchester, Glasgow, and Leith.

Up to the year 1878, wheat was quoted on the English market in shillings and pence per Imperial quarter and bushel. In place of this Dry Measure, certain average weights were substituted, according to which the different qualities of wheat were standardised. These average weights, expressed in English lbs. per Imperial quarter, are—

*Wheat* : 504, 500, 496, 492, and 480

*Rye* : 480, 472, 464, and 456



*Oats* : 336, 320, and 304.

*Maize* : 496 and 480.

Therefore, after 1st January, 1879, corn was quoted in the United Kingdom according to weight and quality. As a unit of weight, 100 lbs. was taken as being equivalent to a cental, and from that time every consignment of cereals unloaded in a British port has been expressed in centals. At first, quotations for wheat and flour per cental were, however, issued only by the Liverpool Exchange. Even to this day, London "spot" quotations for wheat are expressed in Imperial quarters (i.e. for the average weight previously mentioned); and for many years, only dealings in *futures* were expressed in centals.

**London.** The centre of the English trade in cereals is the Baltic Corn Exchange in London; there is also the "London Corn Association"; and for local business, the exchange in "Mark Lane."

For "SPOT" TRANSACTIONS, the "conditions of the grain trade" have to be recognised by the dealers. Wheat is distinguished by the dealers as Russian wheat from Odessa; American Spring and Winter wheats; Danubian, Egyptian, and Chilian wheats; together with Australian and New Zealand wheat, all of which are quoted per 480 lbs.; Leningrad and East Indian wheats, per 492 lbs.; Californian wheat, per 500 lbs.; maize from Odessa and Galatz, 492 lbs.; American maize, per 480 lbs.; rye from the Danubian provinces and the Black Sea, per 400 lbs.; Swedish and Finnish oats, per 336 lbs.; Leningrad, per 320 and 304 lbs.

For the execution of the various kinds of "spot" business, there are about fifty-two different contract forms in use.

"FUTURES" in wheat and maize were introduced by the London Produce Clearing House, the chief business being done in wheat. All dealings in "futures" are based upon American wheats. These refer to American Spring wheats of a quality not inferior to No. 1 Northern Spring (Duluth certificate). The seller can, however, also deliver other sorts, which, according to the testimony of experts, do not weigh less than 60 lbs. per bushel, nor contain more than 3 per cent. chaff. Any difference owing on account of the delivery of inferior qualities is made good by the payment of a sum which is calculated according to a basis fixed by experts. Accordingly, the unit of the contract in wheat for



future delivery is 100 lbs. (i.e. a cental). No contract is made out for a smaller quantity than 4,800 units, and every quantity sold must be a multiple of 4,800.

The price for American wheat is calculated per 100 lbs. net in the sacks of the Dock Company, without discount, and inclusive of the weighing charges and cost of delivery.

A contract in wheat for future delivery is given below. The Sold Note is coloured grey ; the left half is retained by the seller ; and the right half (after being signed by him) is deposited with the Clearing House.

### SOLD NOTE

This part to be left with the Seller.	This part to be delivered at the Office of the Company.
<b>WHEAT CONTRACT.</b>	<b>WHEAT CONTRACT.</b>
LONDON, <i>February 14th</i> , 19..	LONDON, <i>February 14th</i> , 19..
Sold for	To
<i>Blach, White &amp; Co., London</i>	THE LONDON PRODUCE CLEARING HOUSE, LIMITED.
4800 Units, of 100 lbs. each,	4800 Units, of 100 lbs. each,
<b>American Wheat</b>	<b>American Wheat</b>
(Basis No. 1 Northern Spring, Duluth Certificate).	(Basis No. 1 Northern Spring, Duluth Certificate).
<b>Delivery</b> <i>March</i> 19..	<b>Delivery</b> <i>March</i> 19..
<b>Price</b> 6/4 per Unit of 100 lbs.	<b>Price</b> 6/4 per Unit of 100 lbs.
Subject to the Regulations and Conditions of <b>The London Produce Clearing-House, Limited</b> , for Wheat future delivery business.	Subject to the Regulations and Conditions of <b>The London Produce Clearing-House, Limited</b> , for Wheat future delivery business.
<b>Brokerage</b> ½ %	<b>Brokerage</b> ½ %
<i>J. Brown</i> Broker	<i>J. Brown</i> Broker.
	CONFIRMED, <i>Blach, White &amp; Co.</i> Seller.
	REG. NO. : 145.

The Bought Note is coloured yellow ; the left half is handed by the broker to the buyer ; whilst the right half, after receiving the latter's approval, is handed to the Clearing House.



## BOUGHT NOTE

This part to be left with the Buyer. . . This part to be delivered at the Office  
 . . . of the Company.

**WHEAT CONTRACT.****WHEAT CONTRACT.**LONDON, *February 14th*, 19..LONDON, *February 14th*, 19..

Bought for

To  
 . THE LONDON PRODUCE CLEARING  
 . HOUSE, LIMITED.  
 . Bought for

*John Kennedy, London**John Kennedy, London*

4800 Units, of 100 lbs. each,  
                     **American Wheat**  
 (Basis No. 1 Northern Spring,  
   Duluth Certificate).

4800 Units, of 100 lbs. each,  
                     **American Wheat**  
 (Basis No. 1 Northern Spring,  
   Duluth Certificate).

**Delivery**      *March*      19..**Delivery**      *March*      19..**Price** 6/4 per Unit of 100 lbs.**Price** 6/4 per Unit of 100 lbs.

Subject to the Regulations and  
 Conditions of **The London Pro-  
 duce Clearing-House, Limited**,  
 for Wheat future delivery busi-  
 ness.

Subject to the Regulations and  
 Conditions of **The London Pro-  
 duce Clearing-House, Limited**,  
 for Wheat future delivery busi-  
 ness.

**Brokerage**  $\frac{1}{2}$  %  
                     *J. Brown*      Broker.

**Brokerage**  $\frac{1}{2}$  %  
                     *J. Brown*      Broker.

CONFIRMED, *John Kennedy* Buyer.

REG. No. : 145.

**Liverpool.** On the Liverpool Produce Exchange the price of cereals, both for *spot* and *future* transactions, is quoted in shillings and pence per 100 lbs.

In regard to "futures" in cereals, Liverpool plays a leading part, since it keeps in close contact with New York and Chicago, and readily responds to any fluctuations at those places. In the case of wheat futures, American Red Winter, of a quality not lower than the standards of No. 3 or No. 2 Spring, as adopted by the Liverpool Corn Trade Association, must be delivered; whilst in the case of maize, deliveries must be made in American Mixed of a fair average quality. The unit of sale is the cental, and the contract must be for not less than 5,000 centals (i.e. 500,000 lbs.).



Futures in wheat and maize are executed by the aid of a Clearing House which was specially created by the Liverpool Corn Trade Association, Ltd., for the purpose of developing this form of business.

**LIVERPOOL COTTON EXCHANGE.**—The most important cotton market in the world is that of Liverpool, although the imports into the Continent have of late years rapidly increased. Other European centres are Bremen, Hamburg, Havre, and Antwerp.

In dealing in raw cotton, the quality and place of origin of the commodity are important. These are indicated by the Liverpool Cotton Association as follows—

PLACE OF ORIGIN. 1. *North American Cotton*: Sea Island, Florida Sea Island, Upland, Texas, and Orleans.

2. *Brazilian*: Pernambuco, Ceara, Paraibo, Rio Grande, Bahia, Maranham, Santos.

3. *West Indian*: Fiji and Tahiti Sea Island, West Indian.

4. *Peruvian*: Peru rough, Peru smooth, Sea Island.

5. *Egyptian*: Egyptian brown, Egyptian white.

6. *East Indian*: Bengal, Surat.

QUALITY. The cotton is divided into various classes, and to each class is applied a particular name; e.g.

(a) *North American*—

- |                   |                   |
|-------------------|-------------------|
| (1) Ordinary      | (5) Good middling |
| (2) Good ordinary | (6) Middling fair |
| (3) Low middling  | (7) Fair          |
| (4) Middling      |                   |

*Middling* is the average quality, *ordinary* the most inferior, and *fair* the best.

(b) *East Indian*—

- |                   |               |
|-------------------|---------------|
| (1) Middling      | (5) Good fair |
| (2) Good middling | (6) Good      |
| (3) Middling fair | (7) Fine      |
| (4) Fair          |               |

This classification is also used in describing the better grades of Brazilian and Egyptian cotton.

The standards corresponding to the above classes are fixed with great care every year by the Liverpool brokers in conjunction with the cotton factors of the various places of growth. The shipment of the new harvests of North American cotton usually begins



in September, that of Bengal in November, and that of Surat in December.

All kinds of cotton are dealt in on the Liverpool Cotton Exchange. The price is fixed in pence per lb., and a considerable business in "futures" is done in North American cotton. The basis of such transactions is Upland cotton, *middling* quality; and nothing under *low middling* can be delivered.

On the Liverpool Cotton Exchange the following transactions can be concluded—

- (1) "Futures" in North American and Egyptian cotton.
- (2) Sales of cotton warehoused in Liverpool.
- (3) Sales of cotton "to arrive."
- (4) C.F. and C.I.F. sales.

(5) Call business, that is, transactions in which the dealer has the option of buying or calling certain qualities of cotton at a fixed price within a certain period. For the right to exercise this option, a charge is made by the broker.

When the quality of the cotton delivered is unsatisfactory to the buyer, the parties to the contract may resort to *arbitration*. This is usually effected by previously appointed brokers, whose duty is to determine the amount of compensation (if any) to be awarded for default in delivery. For this work, a small charge is made.

**DOCKS.**—A dock may be said to form the connecting link between railway and sea traffic, and provides a means of access for individuals and merchandise passing from one place to another. It is the concentration point of land and sea traffic and must, in addition to providing a sufficiency of railway and siding accommodation, afford ample room for the berthing and standing of vessels. The traffic of the present day is so enormous that these functions must be subdivided to meet the requirements of transport.

Besides separate docks having to be allocated to special traffic, other services such as changing from land to sea traffic, and *vice versâ*, have to be performed. The modern dock must also supply storage accommodation for every kind of commodity; e.g. coal, grain, timber, wool, perishables, and general merchandise.

The accommodation for certain perishable traffic must include markets for its sale—subject to discharge from the ship. This is particularly the case with fish, which entails the establishment of



ice factories and fish-drying grounds. Grain calls for particular plant, such as elevators, and for specialised treatment during storage. Timber demands vast storage yards, with saw mills in the immediate vicinity ; and miles of storage must be provided for coal for shipment. Lastly, passenger traffic requires considerable accommodation, including a hotel, passenger station, and refreshment and waiting rooms. These particular requirements are distinct from those involved in the conduct of ordinary merchandise traffic.

The selection of a site for a dock is governed by engineering requirements, as well as by its proximity to the centres of population which it is intended to serve. Its effective traffic zone by land will depend upon its location, railway access, and freight tariff, coupled with the proximity to, and facilities of, rival ports.

The most important feature to consider in connection with the location of present day docks is the approach to the dock and the depth of the water in the dock. Where possible, the dock must lie alongside a deep water channel, so as to necessitate the minimum amount of dredging, and the depth of water in the dock must be such as to give a draught sufficient for the largest vessel likely to use it. In considering the "lay-out" of the dock, certain factors must be borne in mind, the chief of which are—

(1) *Attention must be paid to the different kinds of traffic with which it is intended to deal.* It is usual to reserve special quaying space or dock accommodation for traffic of various descriptions, but the extent to which this is carried out varies with the size of the dock and the diversity of the traffic dealt in. For instance, general cargoes consisting of ordinary merchandise, require particular quaying and equipment ; cranes of average capacity are required for conveying the goods from the warehouse to the ship, or from the ship to the wagon. The shipment of coal demands special appliances and storage. Grain, which is solely import, requires housing accommodation and dock space for discharging from the vessel to the warehouse.

Timber requires quaying and must be kept separate from other cargo ; whilst fish, owing to particular requirements of the trade, demands accommodation because of its perishable nature. In short, any traffic which attains to such a volume as to be reckoned in shiploads calls for special accommodation.



(2) *The necessity for accommodation for boats awaiting turns at the loading berth.* With regard to the necessity of providing accommodation for boats awaiting their turn to load, the busier the dock, the less the possibility of berthing vessels immediately on arrival. Therefore there must be such central water space to enable boats to obtain quayage space.

(3) *The free and easy passage of boats into and out of the docks.* The constant arrival of vessels renders it essential to have sufficient room to turn and pass along the quays so as to prevent congestion in working.

In order to deal economically with the traffic, it is necessary to utilise part of the dock for the export and part for the import trade. The traffic for shipment enters the reception sidings, where the numbers of the wagons are booked. The wagons then enter the sorting sidings, where they are arranged by shunting engines according as their contents are intended for shipment direct to the quay sides or to the transit sheds.

**EXHIBITIONS.**—Originally, exhibitions were regarded more as a method of education, but later their chief aim has been to advertise different products and to extend their sphere of sale. Arrangements are now made at most exhibitions not only for the purchase of small samples, but also for the execution of large orders from the exhibition itself. More important than the immediate increase of sales, however, are the indirect effects. The exhibition is the means by which the exhibitor's goods are brought to the notice of visitors, and he, therefore, hopes that new business relations will be opened up during the period of the exhibition. To the practical business man, the ideal objects of the exhibition sink into the background—such as the creation of new ideas and impulses, the exposition of the most efficient methods of production, and the general educational effect of the exhibition. Although he may be somewhat indifferent to these results, he himself no doubt receives benefits from them. The primary function of an exhibition to the business man is that of an advertising medium, and its value will be judged by the business world according to the success achieved in this respect. It is true that such a form of advertisement is expensive, since such items as carriage, travelling expenses, ground rent, hotel expenses at the place of the exhibition, insurance, etc., accrue



to the exhibitor, even though his exhibits may not be of a valuable type. In addition, he will have to devise some special means of attracting the attention of visitors to his wares. Whether the expenditure on such an advertisement will lead to a profitable result, one cannot say beforehand. It will easily be seen that whatever sales are actually effected at the exhibition itself cannot be of great weight, and the question arises as to what extent permanent and enduring business connections can be opened up pending the holding of the exhibition. The possibility of permanent results being achieved by this temporary demonstration is not very great. Indeed, the consequences are sometimes quite different from what the exhibitor expected. He may not only exhibit his goods, but at the same time dispose of many secrets of manufacture and specifications of prices which are afterwards imitated and improved upon by foreign competitors. In this case, the exhibition might be the means of assisting foreign competition without extending the sphere of sale of the home producer. This has often been the experience with International Exhibitions, with the result that a feeling of aversion has arisen in many people against such exhibitions, and especially in times of industrial or commercial crises.

The first international exhibition was held in London in 1851, and was known as "The Great Exhibition," although in magnitude it has been greatly surpassed by many others, notably those held in Paris, Chicago, St. Louis, Wembley, and Glasgow. In May, 1939, the World's Fair in New York was opened by President Roosevelt and was visited by millions of people from all parts of the world.

Besides international exhibitions, numerous exhibitions have been held which have limited their operations to a single country or district, or to a special branch of industry. Many persons who regard things in a practical light, have been led to support such exhibitions, since the exhibitors' expenses are not so heavy as in the case of an international exhibition held in some distant town. Moreover, since they are held in the exhibitors' selling area, there is greater opportunity of linking up permanent business connections. When they are well organised and under proper direction, local and specialised exhibitions should, in general, produce favourable results.

**VOLUNTARY ORGANISATIONS IN INDUSTRY AND COMMERCE.**—We find engaged in industry and commerce large numbers of associations



of a voluntary, non-profit-earning character. These organisations are maintained by the voluntary subscriptions of their members, and exist for the purpose of providing them with a variety of services. These associations exist for the benefit of employers and of workers in single trades or groups of trades. They include—

(1) **Chambers of Commerce.** The establishment of Chambers of Commerce in different localities is now almost universal. They are voluntary organisations formed to promote and protect general trade interests, as distinct from trades of a particular class. In Great Britain, they are usually in federation with a general Association of Chambers of Commerce which meets in London. The local Chambers are also in touch with local societies connected with particular trades, and these societies are often directly affiliated with the local Chambers. Not only do the Chambers of Commerce act as a medium for intercourse between commercial men and for the general promotion and protection of their interests, but the government itself takes advantage of their existence in order to obtain as well as to disseminate, useful commercial intelligence and advice.)

Thus Chambers of Commerce may be said to perform much the same general services as the Department of Commerce and Industry of the Board of Trade, although they naturally take a little more personal trouble in the interests of their members. They also perform a number of small services for their members in connection, for example, with certificates of origin, advice as to Customs duties, shipping charges, etc. The London Chamber of Commerce has also a well organised employment department, and has performed a national service in organising a scheme of commercial education, in connection with which it holds annual examinations.

The annual reports issued by Chambers of Commerce are usually of considerable interest and value, as showing the state of affairs of the industries in the part of the country in which they are situated. Chambers of Commerce in smaller towns are, of course, much more closely connected with one or two industries than can possibly be the case with so widespread a Chamber as that of London; and in some very small places they are little more than shopkeepers' associations, working together for the benefit of the trade of the town.

(2) **Trade Protection Societies.** These are associations formed for the purpose of safeguarding the interests of those who are engaged



in trade or in financial matters generally, by giving information as to the stability or otherwise of persons desirous of obtaining credit. For a reasonable membership fee the trader can become a member of one of these societies, which gives him the right to obtain from them, whenever he so desires, confidential reports upon new or old customers. Trade Protection Societies constitute a sort of clearing house for information concerning a prospective customer's reputation. The information is collected through the society's own agents, and is supplemented by such additional information as may be solicited from, or given voluntarily by, undertakings which have had dealings with the people in question.

The three best known mercantile agencies are "Stubbs," "Duns," and "Streets." Each of these has branches in the most important commercial centres of the world. These societies also publish "Mercantile Gazettes," containing information of value to traders such as bills of exchange dishonoured, bankruptcies, judgment summonses issued against debtors, etc., copies being forwarded periodically to subscribers.

(3) **Trade Unions.** A trade union is a continuous association of wage-earners for the purpose of maintaining or improving the conditions of their working lives. At first, these organisations of workers combined in particular trades, and later expanded into whole groups of trades, and endeavoured to attract the whole of the workers belonging to a particular industry. Practically the whole country is systematically covered by the elaborate organisation which the greater unions have wrought out. In every case, the unit is the local branch or lodge, with whose members, in theory, ultimate authority rests. The lodges are usually grouped into districts, served by a paid official; and at the head of all is a national executive with a few permanent officials who take the predominant part in fixing the policy of the whole organisation.

The various methods employed by trade unions may be grouped under two main devices, namely—

- (1) The restriction of numbers, and
- (2) The application of a common rule.

There are various ways of restricting numbers, such as apprenticeship, which was introduced as a way of establishing a control upon the entrants to a trade; and the encouragement of emigration.

The Common Rule is a general term for the attempt to establish



minimum conditions of work and wages independent of the peculiar exigencies of an individual workman or employer. The Common Rule is applied to hours and to conditions of employment as well as to rates of wages. The three methods by which trade unions seek to enforce the Common Rule are legal enactment, collective bargaining, and the payment of Friendly Society benefits.

(4) **Employers' Organisations.** Information about employers' organisations is much less complete than that about trade unions, although the *role* which they play in economic life is equally important. These organisations mostly frame their programmes privately, which enables differences of opinion to be concealed. Again, by not disclosing information about membership, employers' organisations avoid calling attention to weaknesses and disruptive tendencies which may from time to time deplete their ranks. As far back as the eighteenth century there have been 'manufacturers' organisations in England. Adam Smith mentions an organisation of employers for the reduction of wages. With the increase of the power of trade unions, local organisations of employers began to be formed in various sections. In the course of time local organisations serving the interests of particular industries federated. Various associations forming part of these wider organisations fared differently with regard to their influence upon the affairs of the central bodies. Either the individual associations maintained a minimum of independence, leaving all initiative to the central body' or the alliance was a very loose one. The history of employers' organisations in some respects forms a close parallel to that of trade unions, but there are certain differences due to the fact that employers have joined together not only to resist demands of the trade unions for improvements in wages and working conditions, but also to prevent unfair competition amongst themselves by regulating selling price, contract conditions, and other commercial practices and to undertake jointly various commercial, legal, and other services of mutual interest. Thus, the associations may exist for the purpose of—

(a) Scientific research and the co-operative supply of information to members.

(b) The collection of trade statistics from its members.

(c) Legal advice to its members and the drafting of standard forms of contract.



- (d) Joint advertising or joint marketing.
- (e) The control of output or price policy.

Employers' organisations in the different industries have only in comparatively recent years set up machinery for the co-ordination of their activities. Also, whereas the trade union movement has concentrated the functions of co-ordination almost entirely in the Trades Union Congress, the employers have established two bodies for this purpose—*The National Confederation of Employers' Organisations* for labour matters, and the *Federation of British Industries* for economic and commercial questions. Employers also co-operate in such organisations as the Association of British Chambers of Commerce, and the Chamber of Shipping, the chief objects of which are to consider questions concerning commerce, manufactures, and shipping; to collect and disseminate information on these questions; to undertake the settlement by arbitration of disputes arising out of commercial transactions; to bring the opinions of the Associations before Parliament; and to promote or oppose legislation in Parliament.

**SOCIAL ORGANISATIONS.**—A fourth group of voluntary organisations concerns itself with spheres of activity outside of the economic life of the community. These include many associations of fundamental importance in the life of organised society in connection with religion, politics, science, and the arts. These societies, again, are of a non-profit type, though they are obliged to concern themselves with economic matters to a certain extent since their activities call for the raising and spending of an income. These organisations include—

(1) **Educational Organisations.** The chief burden of education at the present day falls upon the State, but in certain directions still educational facilities are provided by voluntary effort. This is particularly the case in the sphere of adult education where many voluntary organisations exist, which have as their object the turning of the worker's leisure time to constructive use.

(2) **Political Organisations.** Although the principles and historical development of the political parties vary greatly in the different countries of the world, yet in the main, a three-fold division of parties can at present be distinguished—

- (a) Those who represent the interests of land-ownership.



(b) Those supported by industry and commerce.

(c) Those representing labour.

The familiar lines of demarcation between political organisations have become more indistinct of recent years. Each party has an association for the protection of its interests. The objects of such an organisation usually include the organisation of party meetings and propaganda, the provision of social and educational facilities for its members, and the securing of the proper registration of the voters in a district.

### TEST PAPER XLI

1. Mention some of the institutions which are engaged in the furtherance of trade.

2. Give examples to show the different meanings sometimes attached to the term "market."

3. Which is the simplest form of a market?

4. Enumerate the advantages of annual fairs in connection with the Wholesale Trade, and mention some of the centres where they are still held.

5. What are the chief characteristics of a modern Exchange?

6. Name some of the methods of describing goods which are sold on an Exchange.

7. Business on the Exchanges is effected for goods which are to be delivered at different periods. Mention some of these periods.

8. Say what you know of the organisation of the Corn and Cotton Exchanges.

9. What is a dock? State some of the factors which must be borne in mind in considering the "lay-out" of a dock.

10. Explain briefly the objects of a Chamber of Commerce.

11. State the chief advantages and disadvantages of International Exhibitions as an advertising medium.

12. Distinguish between a produce exchange and an ordinary market or fair. What commodities are suitable for dealings on an exchange, and why?

13. What useful purposes are served by modern business fairs and exhibitions? Illustrate your answer by reference to any exhibition which you have visited or heard about.

14. What are the functions of a Trade Protection Society?

15. "The object of a trade union is always to maintain or improve the conditions of employment of its members." In what way does it contrive to achieve this end?

16. Say what you know of Employers' organisations in Great Britain. What useful purpose do they serve?

17. Name six voluntary organisations of a non-profit-earning character. In each case state whether it is primarily economic or social.

### ABBREVIATIONS USED IN TRADE

<b>A/S</b>	. . Account sales
<b>A/C</b>	. . Account current
<b>Ad val.</b>	. . <i>Ad valorem</i> (according to value)
<b>A/o</b>	. . Account of
<b>Appro.</b>	. . Approval

<b>A/T</b>	. . American terms (grain trade)
<b>@</b>	. . At; for; to; from
<b>B/</b>	. . Bag; bale
<b>Bar.</b>	. . Barrel
<b>B/d</b>	. . Brought down



ABBREVIATIONS USED IN TRADE—*contd.*

<b>B/f</b> . . . Brought forward	<b>I.B.I.</b> . . . Invoice Book in-wards
<b>c. &amp; f.</b> . . . Cost and freight	<b>I.B.O.</b> . . . Invoice Book outwards
<b>C/N</b> . . . Credit note	<b>Id.</b> . . . Idem—the same
<b>C/</b> . . . Case; currency	<b>i.e.</b> . . . <i>Id est</i> —that is
<b>Cs.</b> . . . Cases	<b>Inst.</b> . . . Instant—of the present month
<b>C/d</b> . . . Carried down	<b>I.W.</b> . . . Isle of Wight
<b>C/f.</b> . . . Carried forward	<b>J.A.</b> . . . Joint Account
<b>Cert. Inv.</b> . . . Certified invoice	<b>Kilo.</b> . . . Kilogramme
<b>Ch. fwd.</b> . . . Charges forward	<b>£T.</b> . . . Pound Turkish
<b>Ch. ppd.</b> . . . Charges prepaid	<b>£E.</b> . . . Egyptian pounds
<b>C.i.f. &amp; c.</b> . . . Cost, insurance, freight, and commission	<b>L.m.c.</b> . . . Low middling clause (cotton)
<b>C.i.f. &amp; i.</b> . . . Cost, insurance, freight, and interest	<b>M/m</b> . . . Made merchantable
<b>C.i.f.c. &amp; i.</b> . . . Cost, insurance, freight, commission, and interest	<b>M/u</b> . . . Making up (price)
<b>Con.</b> . . . Contra (against)	<b>MM.</b> . . . Messieurs, sirs
<b>Con. Inv.</b> . . . Consular invoice	<b>M/R</b> . . . Mate's Receipt
<b>Csk.</b> . . . Cask	<b>MSS.</b> . . . Manuscripts
<b>C.w.o.</b> . . . Cash with order	<b>N.B.</b> . . . Take note—mark well
<b>C.H.</b> . . . Custom house	<b>Nos.</b> . . . Numbers
<b>C.W.S.</b> . . . Co-operative Wholesale Society	<b>O.D.O.</b> . . . Outdoor Officer (Customs)
<b>D.bk.</b> . . . Drawback	<b>P/A</b> . . . Power of Attorney
<b>Deb.</b> . . . Debiture	<b>P.L.A.</b> . . . Port of London Authority
<b>D/O</b> . . . Delivery order	<b>Pcs.</b> . . . Pieces (of cloth)
<b>E. &amp; O.E.</b> . . . Errors and omissions excepted	<b>P/C</b> . . . Price current; petty cash
<b>E.E.</b> . . . Errors excepted	<b>Pkg.</b> . . . Package
<b>E.g.</b> . . . <i>Exempli gratia</i> (for example)	<b>P.P.S.</b> . . . A further postscript
<b>Encl.</b> . . . Enclosure	<b>Qty.</b> . . . Quality
<b>Exors.</b> . . . Executors	<b>Qr.</b> . . . Quarter
<b>Exs.</b> . . . Expenses	<b>q.v.</b> . . . <i>Quod vide</i> —which see
<b>F.a.q.</b> . . . Fair average quality	<b>R.</b> . . . Rupees
<b>Fco.</b> . . . Franco (free)	<b>rm.</b> . . . Ream
<b>F/d</b> . . . Free docks	<b>s/d</b> . . . Sea-damaged (grain trade)
<b>F.l.b.</b> . . . Free into bunker (coal trade)	<b>seq.</b> . . . The following
<b>F.O.</b> . . . Firm offer	<b>Sks.</b> . . . Sacks
<b>F.o.c.</b> . . . Free of charge	<b>S.O.</b> . . . Seller's option
<b>Fol.</b> . . . Folio	<b>Spec.</b> . . . Speculation
<b>F.o.T.</b> . . . Free on Trucks	<b>Sq.</b> . . . Square
<b>F.g.</b> . . . Fully good	<b>S.W.</b> . . . South-west
<b>Gaz.</b> . . . Gazette	<b>T.D.</b> . . . Tilbury Dock
<b>G.m.b.</b> . . . Good merchantable brand	<b>T.E.</b> . . . Trade expenses
<b>G.m.q.</b> . . . Good merchantable quality	<b>T.M.O.</b> . . . Telegraph money order
<b>G.o.b.</b> . . . Good ordinary brand	<b>Ult.</b> . . . Ultimo—of the last month
<b>Gr.</b> . . . Gross	<b>V.D.</b> . . . Victoria Docks
<b>Grs.</b> . . . Grains	<b>Via</b> . . . By way of
<b>Hhd.</b> . . . Hogshead	<b>W/B</b> . . . Way bill
<b>H.P.</b> . . . Horse-power	<b>Wd.</b> . . . Warranted
<b>I.B.</b> . . . Invoice Book	<b>W.I.</b> . . . West Indies
	<b>Yds.</b> . . . Yards



# SECTION V—EXCHANGE, BANKING AND FINANCE

## CHAPTER XLII

### MONEY AND EXCHANGE

THE next branch of commerce, and the one which is most closely connected with trade itself, is that of banking and the mechanism by means of which exchanges are effected. It has already been seen that division of labour implies the possibility of exchange. A certain miner may spend the whole of his time in the production of coal, simply because it can be exchanged for other commodities. Through the medium of exchange, the miner receives a large increase in utility, since he parts with his superabundant commodity and receives in return goods of which he is in want, and which yield him greater satisfaction. A change of ownership of goods is, therefore, a means of increasing utility and of conferring the power to satisfy human desires.

**ADVANTAGES OF EXCHANGE.**—The negress who goes to market with her basket of coco-nuts sells them in exchange for cowrie shells, which serve as money in West Africa. With these shells, she is enabled to obtain a variety of articles which, to her, are of greater value than the coco-nuts she has parted with. On the other hand, the party who bought the coco-nuts and gave shells in return must also have received a greater value, as otherwise he would not have made the exchange. Since both parties gain an advantage, the exchange is productive. In fact, in every transaction, both the buyer and the seller acquire an increase of utility, although the use of money conceals the real nature of the operation.

The negress who has an abundance of coco-nuts does not sell for the sake of selling, but in order to acquire something which will satisfy her needs. This is precisely the same in a more advanced stage of trade. The trader of the present day aims at selling at a profit, which represents the increase of utility resulting from his exchange operations.



Although the trader is usually represented as a seller, it is important to remember that he only sells in order to acquire something of greater value in return. For example, a person buys a ream of paper from a retail shop for 10s. In return for his 10s. he receives a utility of at least equivalent value, whilst the trader may be said to have bought the money by handing over the goods. In return for the money, the paper dealer may obtain increased supplies of paper of which he is in need. In this way, both the customer and the trader have effected their exchanges through the medium of money, and both have received an increase of satisfaction in consequence of the exchange.

**DEFINITION OF MONEY.**—It will be seen from the above illustration that money is chosen to measure the *values* of other commodities, just as a yard measure is used to measure the *length* of a commodity. Money also facilitates exchanges by avoiding the difficulties of barter. These are—

(1) The difficulty of each person having to find someone who not only desired what he had to sell, but was also willing to give him what he, in his turn, wanted in return for it.

(2) The determination of the rate at which exchange shall take place.

Both these difficulties are removed by the intervention of money, which may be defined as: "A THIRD COMMODITY, CHOSEN BY COMMON CONSENT TO BE A MEANS OF EXCHANGE AND A MEASURE OF VALUE BETWEEN EVERY OTHER TWO COMMODITIES."

**EVOLUTION OF MONEY.**—Since money is a commodity chosen by common consent, it follows that any commodity may be chosen. From the earliest times, many articles have been used in different countries, such as skins, cattle, furs, cowrie shells, tobacco, opium, iron, tin, copper, and salt, as well as the precious metals. There seems to have been a particular form of money in common use amongst the people in each of the four great stages through which mankind has evolved, viz. : (1) Hunting and Fishing ; (2) Pastoral ; (3) Agricultural ; and (4) Commercial.

**The Hunting Stage.** In this stage, the skins of wild animals were used as money. Reference is made to this stage of economy, in the following passage, which occurs in the Book of Job (Chap. ii, v. 4) : "Skin for skin ; yea, all that a man hath will he give for his life." At this period, skins were the recognised medium of



exchange, and a man was willing to give up his last skin rather than lose his life.

**Pastoral Stage.** In this stage, man roams over land which is still ownerless. On it he feeds his cattle and then drives them on to fresh pastures. His main possessions are, therefore, his flocks and herds: these constitute his wealth, and cattle are his money. Among the Anglo-Saxons, slaves and cattle are spoken of as living money. In most countries, cattle were probably the earliest form of money, that is to say, goods were valued at so many cattle. When metal money was first introduced, some of the earlier coins had cattle stamped upon them. Thus *pecus* (cattle) is the origin of the Latin *pecunia* (money), and of our English word "pecuniary"; and the word "cattle" itself is derived from "capital," the origin of which is the Latin word *caput* (head), beasts having from the earliest times constituted the chief part of a man's property.

**The Agricultural Stage.** This stage evolved when the people settled down to cultivate the land, and thus abandoned their roaming habits. In this stage, people discovered that it was easier to dig with a metal spade than with a wooden one. Hence, bronze and iron became general commodities, and these were soon adopted as money. The money of the Spartans, for instance, was made of iron.

**The Commercial Stage.** During this stage the precious metals emerged as the chief form of money. "By a tacit concurrence," says J. S. Mill, "almost all nations, at a very early period, fixed upon certain metals, and especially gold and silver, to serve this purpose. No other substances unite the necessary qualities in so great a degree, with so many subordinate advantages. Next to food and clothing, and in some climates even before clothing, the strongest inclination in a rude state of society is for personal ornament, and for the kind of distinction which is obtained by rarity and costliness in such ornaments. After the immediate necessities of life were satisfied, everyone was eager to accumulate as great a store as possible of things at once costly and ornamental, which were chiefly gold, silver, and jewels. These were the things which it most pleased every one to possess, and which there was most certainty of finding others willing to receive in exchange for any kind of produce."



Thus, the evolution of gold and silver as the principal form of money is an illustration of the law of the "survival of the fittest," since these metals possess qualities which have enabled them to survive.

**FUNCTIONS OF MONEY.**—The chief functions to be performed by the substance which is chosen by common consent to act as money are—

(1) To act as a medium of exchange, that is, to be universally acceptable and to do away with the difficulties of barter.

(2) To be a measure of value, that is, something in which the value of other commodities can be measured and compared.

(3) To act as a "standard for deferred payments," that is, something in terms of which the amount to be paid at a future time can be correctly expressed to the satisfaction of the parties making the contract.

(4) To be a "store of value," that is, something in which the means of buying other commodities, or "purchasing power," can be retained.

**CHARACTERISTICS OF A "GOOD" MONEY.**—The commodities which most accurately perform the "Functions of Money" fulfil the requisites of a "good" money. The attributes of gold and silver are such as to fit them to serve in a peculiar manner as the standard money in most civilised countries. These attributes, according to Jevons, are: Value, Portability, Divisibility, Indestructibility, Homogeneity, Stability of Value, and Cognisability. They may be remembered more easily by arranging them so that the first letter of each word will give, as useful mnemonics, the words "Dish" and "Cup." Thus, the qualities of a "good" money are—

**Divisibility.** Gold and silver are eminently divisible, and, when pure, they are always of the same quality. Unlike diamonds and other precious stones, they are capable of reconstruction without loss of value.

**Indestructibility.** Gold and silver do not deteriorate through exposure to the air, nor do they require great care for their preservation. They do not corrode, but iron does. Indeed, they are among the most imperishable of all substances.

**Stability of Value.** No substance is perfectly stable in value as a commodity, since there are always some changes in supply.



Gold is, perhaps, the least variable, and for this reason has become the leading monetary standard.

**Homogeneity.** Since gold and silver coins bearing the same denomination are all equally good, there is no inducement to choose one unit of the metal rather than another. Precious stones do not possess this attribute.

**Cognisability.** There is no difficulty in recognising a gold coin, and it may be distinguished from other coins by almost any of the senses. In the case of jewels, an expert would be required to determine their value.

**Utility.** As a substance, gold is much desired for purposes of personal adornment. It is difficult to produce, and is, therefore, likely to maintain its value.

**Portability.** In the case of gold, a great value is contained in small bulk, so that there is no difficulty in carrying the metal about, because of its weight. In consequence, it is easily hidden, which is still a consideration of some importance in times of insecurity.

**CURRENCY SYSTEM.**—The currency of a country consists of anything which is used as a medium of exchange in effecting purchases and sales, and in discharging debts and other obligations. It is said to be in a normal state when—

(1) The current coins are struck from metal, the exchange value of which is practically equivalent to that stamped on the face of them.

(2) The payer is obliged to give and the payee is entitled to receive current money.

(3) The note-issuing banks are always under the obligation to meet their notes by the payment of current money, without any charge being imposed for so doing.

(4) The "token" coins correspond in amount to the requirements of the community.

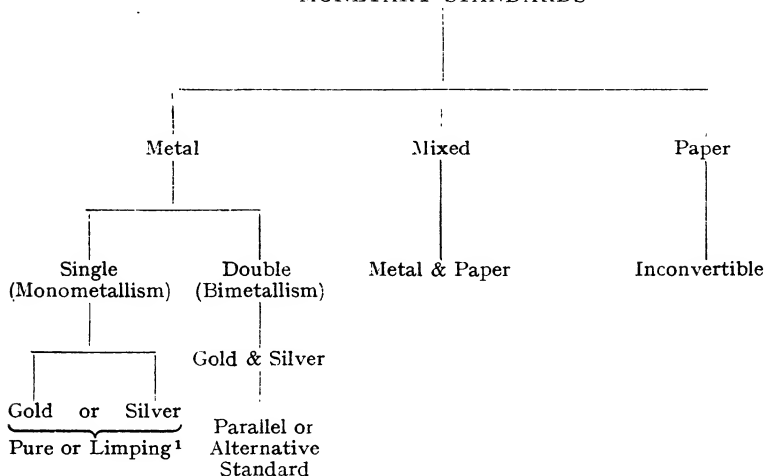
(5) The coining of current coins can be effected freely and without hindrance for public or private purposes.

**MONETARY STANDARDS.**—Although a variety of commodities has been used, at one time or another, in the capacity of money, the precious metals—gold and silver—have proved the most satisfactory, and have formed the basis of most monetary systems. It is true that the events of recent years have served to bring metallic



standards, and particularly those based on gold, into some disrepute, but no satisfactory alternative, free from practical difficulties, has as yet been devised. A country may link its basic currency unit, that is, its unit of account, to one metal, and in that case it is said to be on a *monometallic standard*. Thus, in England before the War, gold was the only standard, as it circulated at its face value, was legal tender to any amount, and could be brought to the Mint for coinage by any individual. It is not necessary that

### MONETARY STANDARDS



the standard metal actually be embodied in a coin; it is sufficient if the circulating medium, such as a paper note, is convertible into the metal at a fixed rate. If the currency unit is based upon two metals, such as gold and silver, then it is said to have a *bimetallic standard*. Since the War, this latter standard has almost passed from use, but the abandonment of the gold standard by a large number of countries in 1931 and 1932 has served to re-awaken interest in it.

**The Gold Standard.** Of all the metals which have, from time to time, acted as monetary standards, gold has been the most important. Its pre-eminence seems to be derived principally from two circumstances—the physical properties of the metal and its scarcity,

<sup>1</sup> A Limping Standard is one in which silver and gold are full legal tender, but only gold is freely coined,



the combination of which has made it highly suitable as a store of value and as a medium of exchange. Only during the past hundred years, through the transition from a hoarding to a credit economy, has the fundamental importance of gold as a means of payment tended to disappear into the background. The gold standard, as distinct from the use of metallic gold for the settlement of debts, is essentially a nineteenth-century invention. A country is said to be on a gold standard when the following conditions are fulfilled—

(1) The standard currency unit must be defined by law as a fixed weight of gold of a specified fineness. Thus, the franc is said to be the equivalent of 65.5 mg. of gold, nine-tenths fine.

(2) This gold unit, or its representative, must be made full legal tender in the settlement of debts.

(3) The issuing authority must be prepared to convert the circulating medium into gold, or *vice versa*, at a fixed rate, though it may fix a minimum amount for conversion.

(4) There should be full freedom for the import and export of gold.

The gold standard is not a fixed and rigid mechanism, but a system of monetary and credit policy which has been adopted in varying forms to suit local needs. Never in history has the gold standard been simultaneously applied in exactly the same manner in all the countries which are roughly classified as adhering to it. The following systems may be recognised—

(1) *Full Gold Standard*, which is sometimes styled the Gold Specie Standard, and was in force in this country before 1914. The outstanding feature of this system is that coins of the standard metal circulate freely as media of exchange. There may be also a circulation of notes, but these must be exchangeable freely for gold coin. Moreover, any person holding gold bullion must have the right of free mintage into coin. Finally, there must be no limitations on gold movements. This system practically disappeared in later years, since it is unnecessarily expensive and is not required for the preservation of public confidence in a developed commercial community.

(2) *Gold Bullion Standard*. This variation was introduced by Great Britain in 1925, when a system was introduced whereby the circulation of gold coin and the convertibility of notes into gold coin was abandoned. The unit of account is a paper note which



is convertible into gold bullion at a fixed rate. In this way, gold would not be used for internal circulation, but could be obtained in bar form for making payments abroad. A further restriction was the fixing of a legal minimum quantity of gold below which the Bank was not bound to sell. Following the example of England, a number of other countries adopted the same system, since it economises gold reserves and is more cheaply administered.

(3) *Gold Exchange Standard* under which the circulating medium is a paper note. These notes are convertible at a fixed rate into "gold exchange" in the form of bills of exchange and other credit instruments, payable in a gold standard centre where gold reserves actually exist. As a rule, the reserves of the currency authority operating this system consist of gold and foreign exchange convertible into gold. The central bank must hold itself open to deal in foreign exchange at fixed rates and must regulate the volume of the internal currency so as to maintain convertibility. This standard, although it has offered possibilities of economy in the use of gold, has also complicated the mechanism of the international gold standard system.

(4) *Flexible Gold Bullion Standard*. This is the name sometimes given to the system now operated by the United States of America. The U.S.A. temporarily abandoned the gold standard in April 1933, and under the provisions of the Agricultural Adjustment Act, 1933, the President was given power to devalue the dollar up to 50 per cent of the former value. As from 1st February, 1934, the value of the dollar was fixed at 59.06 per cent of its former value, so that the dollar is now equal to  $15\frac{5}{16}$  grains of gold nine-tenths fine. This figure was chosen so that the new price for gold should be exactly \$35 per fine ounce. The Treasury was authorised to buy all gold offered to it at \$35 per fine ounce and could sell gold at this price if the dollar touched gold export point. This parity is not necessarily permanent, since the President has power to vary the gold content within a range of 50 and 60 per cent of the former value. This "variable parity" introduces a factor of uncertainty into the position which is out of harmony with a satisfactory international standard.

**The Silver Standard.** Throughout the ages, silver, like gold, has been counted amongst the precious metals, though its comparative abundance has usually given it the second place in the estimation



of mankind. Yet, since the middle of the eighteenth century, silver has been gradually displaced by gold for monetary purposes, although to-day, on account of dissatisfaction with the gold standard, the rehabilitation of silver is once more being discussed. Even to-day, however, it should be remembered that the part played by silver is by no means unimportant. It is still the standard of value in China and some few other, though less important, areas, and constitutes an important "store of value" in India as well as China. In recent years, silver has been far from satisfactory as a money material on account of its great instability of value. With the exception of the War period, the trend of silver prices has been downward for the past sixty years; whilst from 1920 to 1931, silver prices dropped almost continuously. The following causes may be said to have contributed to this fall—

(1) The price of silver was, in part, influenced by the same factors as all other commodities which declined in price over the same period. This is not a complete explanation, however, since the general price level fell by 33 per cent between 1924 and 1930, whilst the price of silver fell by 48 per cent.

(2) The demonetisation of silver by many European countries and the reduction of the silver content of the subsidiary coinage, as in this country, caused additional supplies of silver to come on the market.

(3) The Indian Government held large stocks of silver not required for currency purposes, and the presence of these helped to spoil the market.

(4) Silver is produced jointly with other metals, such as lead, copper, and zinc, so that a fall in price does not check production to an appreciable extent.

(5) The demand for silver, both for coinage and industrial purposes, has tended to diminish.

This instability in the price of silver has had serious consequences upon the trade of China, and has been detrimental to the interests of silver producers. An attempt was made at the World Economic Conference in 1933 to arrive at an agreement and to reconcile the conflicting interests involved. The Americans and the silver producers aimed at a rise in the price of silver; the Chinese Government wanted stabilisation, and the Indian Government was anxious to dispose of its stocks. The agreement concluded at the Confer-



ence provided that the Indian Government was to restrict its sales to 35,000,000 ounces a year for the next four years, while four other Governments, of which the American was the chief, agreed to purchase this amount. This agreement could be interpreted as a *stabilisation measure*.

In May, 1934, however, under pressure from the American producing interests, the U.S.A. introduced a Silver Purchase Act. This measure declared it to be the intention of the U.S. Government to purchase silver until its monetary reserves consisted as to three-quarters of gold and as one-quarter of silver. In August, 1934, the President issued a proclamation calling on all holders of silver in the U.S.A. to sell their stocks to the Treasury at a fixed price of 50·01 cents per ounce. The Treasury also commenced to buy silver from abroad and forced up the price. This move embarrassed China by causing a rise in the value of her silver currency, and creating a drain of silver from the country. In order to prevent this, China imposed an export duty on silver, which can be increased if the price of silver rises further, and so discourage the export of silver from China by making it unprofitable.

**Bimetallism.** This system was traditional in Europe for many centuries and was abandoned on the Continent only after the Franco-Prussian War. In its simplest form, bimetallism entails the convertibility of legal tender notes or coins into fixed quantities of either gold or silver at the option of the holder, and the acceptance of unlimited quantities of either metal by the currency authority in exchange for legal tender at the fixed Mint price. Where two metals are used in this way as unlimited legal tender, it is possible for the exchange value of the one in terms of the other either to be defined by law, or to be left to the play of demand and supply in the market. In the latter case, where the relative values of the metals depend upon their market prices, we have what is called a *parallel standard*. But, in a modern State, it is essential for the purpose of long-term contracts that the market ratio shall be legally fixed. Hence what is known as the *alternative standard* is the only form which is practicable.

The events of recent years have caused some revival of interest in the question of bimetallism, which finds support upon three main grounds. The first is the natural desire of silver producers to discover a new and profitable market for their product. Secondly, it



is claimed that trade suffers as between silver standard and gold standard countries when the value of silver falls considerably in terms of gold. Finally, it is argued that stocks of gold are not sufficiently great to permit of an international gold standard without the support of a second metal. One of the principal claims for the system is that it would confer greater stability of prices on account of what is termed the compensatory action of bimetallism. This arises from the principle that the relative values of any two commodities may be kept constant, provided that they can be treated as perfect substitutes. The act of substitution is performed by a debtor who, under a bimetallic regime, is permitted to discharge any debt payable in legal tender either in gold or silver at his option. If, at any moment, one of the two metals is more cheaply obtainable in the market, it will be chosen for the purpose. The demand for the cheaper metal will increase and that for the dearer metal will fall off, thus setting up a reactionary movement in relative values. The difficulties in the way of the scheme may be summarised as follows—

(1) The difficulty of reaching a general agreement on the subject between a large number of countries whose interests are conceived as being widely different.

(2) The selection of a suitable Mint ratio for the values of the two metals.

(3) The fact that the advantages claimed for the system could never be realised unless a sufficiently large number of countries adopted it.

#### **INFLUENCE OF THE WORLD WAR ON CURRENCY CONDITIONS.—**

The outbreak of the war brought a radical change in the currency conditions of nearly every civilized State, not only of the belligerent powers, but also of the neutrals. During the first few years of the war most States discharged their note-issuing banks from the obligation of paying their notes in gold. The export of gold was prohibited, the internal circulation of gold was either greatly restricted or completely abolished, and a free money market in Europe ceased to exist in August, 1914, whilst the United States was able to maintain its gold currency only in the face of great difficulties.

The principal landmarks in the development of British currency since the termination of the war in 1918, are as follows—



**(1) THE ADOPTION OF THE "CUNLIFFE LIMIT" IN 1920.**—Pursuant to a recommendation of the Cunliffe Committee, which was appointed after the war to investigate into the prevailing currency conditions, a limit was imposed upon the currency note issue. A Treasury note minute of 15th December, 1919, prescribed that the fiduciary issue of currency notes in any year should not exceed the maximum fiduciary issue recorded in the preceding year. The actual maximum recorded for 1919 was £320,600,000, and accordingly this became the prescribed maximum for 1920. Under this rule the limit can decrease, but cannot increase. Hence, the adoption of the "Cunliffe Limit" put an end to currency inflation, and with the gradual diminution in the number of notes issued since 1920 a policy of deflation has resulted.

**(2) RESTORATION OF THE GOLD STANDARD IN 1925.**—On 28th April, 1925, the Chancellor of the Exchequer announced that the export of gold would be free, and at the beginning of May was passed the Gold Standard Act, imposing on the Bank of England the obligation to sell gold bullion (in bars of 400 oz. troy) at the par price of £4 4s. 11 $\frac{5}{11}$ d. per fine ounce, or £3 17s. 10 $\frac{1}{2}$ d. per standard ounce.

The obligation to redeem currency notes in gold coin was repealed and so was the free coinage of gold by the Mint. Thus, the Act provided for the free convertibility of pounds into gold in the form most convenient for the world market, but interposed a bar to the issue of gold coin for active circulation. Currency notes remained the principal legal medium of exchange, and Bank of England notes were convertible into currency notes. The substitution of Bank of England notes of £1 and 10s. for the currency notes, as recommended by the Cunliffe Committee, was provided for by the Currency and Bank Notes Act, 1928.

**(3) CURRENCY AND BANK NOTES ACT, 1928.**—The Act terminated the dual control of the note issues of this country by the Bank of England and the Treasury which had existed since 1914, in accordance with the well-established principle that the Central Bank, and not the Government, should be the note-issuing authority. The amalgamation of the note issues was recommended by the Cunliffe Committee and also by the Gold Standard Committee. According to the provisions of this Act—

(1) All outstanding currency notes issued under the Currency and



Bank Notes Act, 1914, were to be transferred to the Issue Department, such notes being thereafter deemed bank notes.

(2) Currency notes were to continue to circulate until they were exchanged for bank notes, and both £1 and 10s. notes to be issued by the bank were to be legal tender for any amount in England, Wales, Scotland, and Northern Ireland just as currency notes had been.

(3) The amount of the fiduciary issue of the Bank was fixed at £260 millions. There is, however, a provision that, by agreement with the Treasury, the Bank's fiduciary issue may, if necessary, exceed that limit. This provision was inserted to meet the views of those who thought that the supply of currency might be insufficient to meet the legitimate requirements.

(4) Assets from the Currency Notes Redemption Account and other securities representing in the aggregate the amount of the transferred currency notes, were to be transferred by the Treasury to the Bank in consideration of its undertaking the liability for the repayment of the notes.

(5) Banks in Scotland and Northern Ireland were empowered to hold bank notes instead of gold as cover for their notes in circulation.

Thus, in conformity with the provisions of this Act, the Bank of England became the sole note issuing authority, the profits on the currency note issue, which the Treasury had hitherto made, were to continue to accrue to it; and, in addition to the profits on the £1 and 10s. notes, it was to receive the profits from the rest of the Bank's note issue. Formerly, the Bank had kept these profits, but the Court of Directors, being of opinion that it was not desirable that the profits of a note issue should go into the pockets of a privately owned institution, decided, as from the date of the transfer of the Treasury issue, to hand over all the profits to the Exchequer.

**(4) ABANDONMENT OF THE GOLD STANDARD, 1931.**—The example of Great Britain in restoring the gold standard was followed, at intervals, by other leading commercial nations. It speedily became evident, however, that the standard was not functioning as it had done before the War, largely on account of such disturbing factors as tariffs, War debts, and reparations payments. In 1931, a number of events served to undermine foreign confidence in the financial position of the City of London. There were banking difficulties in Germany and in other Central European countries, and it was known that British bankers had made large short-term loans to



these countries. Again, the *Macmillan Committee*, in its report published in July, 1931, had drawn attention to the magnitude of the short-term claims on London. A little later the May Committee published its report upon the condition of the public finances, and for the first time there was a general realisation of the probability of a large deficit, estimated at £120 millions. Throughout August and early September there was a withdrawal of foreign funds which gathered in intensity. On 21st September, the *Gold Standard (Amendment) Act* was passed, suspending the Bank of England's obligation to sell gold.

The fall of the pound caused the abandonment of the gold standard by a number of countries which were in close relationship with Great Britain. In a very short time a large number of the world's currencies were on an inconvertible basis, and measures of exchange control and restriction were growing apace. The international gold standard suffered a further loss of prestige when the U.S.A. abandoned it in 1933, and although she re-introduced it in 1934 after devaluing the dollar, her action has served to intensify rather than relieve the monetary troubles of the world.

**RECENT MONETARY DEVELOPMENTS.** For some years after the breakdown of the international gold standard in 1931, the countries of the world were divided into two broad groups in regard to their monetary arrangements. In the first place there were those who had abandoned the gold standard for the time being and allowed their currencies to depreciate. On the other hand, there was a small group of countries, of which France was the most important, who still maintained the value of their currencies in terms of gold on the former basis and were prepared to make considerable sacrifices to maintain it. As time went on, the divergence in the economic situation of these two groups became very marked. In the former group, the devaluation of currencies had produced easy money conditions and low interest rates, so that industry began to revive and unemployment to fall. In the second group, however, the deflationary pressure continually increased and the economic situation went from bad to worse.

(1) **THE TRIPARTITE AGREEMENT.**—In September, 1936, the position could be maintained no longer and the French Government announced the devaluation of the franc, a line of action which was speedily followed by the remaining members of the "Gold Bloc."



Simultaneously with the announcement of the devaluation of the franc, the British, French, and United States Governments subscribed to a declaration of policy which has subsequently become known as the *Tripartite Agreement*. They announced their intention to co-operate closely in an effort to restore order in international economic relations, and to use the appropriate available resources, so as to avoid, as far as possible, any disturbance of the basis of international exchange resulting from the readjustment of the franc. In October, the three Governments announced the provisional establishment of a gold market between their exchange equalisation accounts.

This new arrangement, although it marked a step forward in international monetary co-operation, was in no sense a re-establishment of an international gold standard. The parties to the agreement were prepared to co-operate on a day-to-day basis, but were not prepared to give to their currencies a definite gold value. At the same time, the agreement staved off the possibility of a competitive depreciation of currencies, and in May, 1938, when the French Government discovered that a further devaluation of the franc was necessary, this was effected after consultation with the other parties to the Tripartite Agreement.

(2) **CURRENCY AND BANK NOTES ACT, 1939.**—This Act simplified the interlocking arrangements between the Exchange Equalisation Account and the Issue Department of the Bank of England. It provided for the valuation of the gold stock of the Issue Department at current values and fixed the Fiduciary Issue of the Bank at £300 million. Thus, in future the assets backing the Bank of England's note circulation, that is gold and securities, are to be revalued each week at market prices, and any discrepancy between the resulting figure and the amount of notes outstanding is to be remedied, not as hitherto, by adjusting the issue to the backing, but by exactly the reverse process, namely—diminishing or increasing that backing as the case may be, through transfer of gold or securities to or from the Exchange Equalisation Account. In future, therefore, the outstanding volume of notes issued will be the determining factor and the note issue is no longer to be determined automatically by changes in the volume of gold reserve. The change is the symbol of the tremendous reaction which has occurred from the rigid ideas of the Currency School which found their expression in the Bank



Charter Act of 1844 to the elasticity of the new currency management towards which we are tending to resolve.

(3) **WAR-TIME CURRENCY MEASURES.**—Under powers conferred by the Currency (Defence) Act, 1939, the gold reserved in the Issue Department of the Bank of England was transferred to the Exchange Equalisation Account upon the outbreak of war. The transfer of gold had to be accompanied by a corresponding expansion in the fiduciary circulation from £300 millions to £580 millions. The amount of the Fiduciary Issue has been increased from time to time, as the demand for currency has grown, and at the end of 1941 was £780 millions.

### TEST PAPER XLII

1. An Englishman exchanges a rifle and two flasks of whisky for 10 furs. Which party gains in the exchange ?
2. Name the difficulties of direct barter.
3. "Money permits our specialised effort to be turned into generalised enjoyment; we may say that each one of us is a factor in specialised production, and that the money we get entitles us to generalised consumption." Explain and elucidate.
4. Trace the evolution of money through its various stages.
5. What do you understand by a measure of value ?
6. What are the requisites of a good standard of value ? How far does the present British monetary system fail in supplying a proper standard ?
7. What are the characteristics of a normal currency system ?
8. Copy the diagram on page 486, and explain carefully the different forms taken by a monetary standard.
9. What is meant by "The Gold Exchange Standard" ? Describe concisely the circumstances under which this monetary system came into being, and indicate the general principles on which it is based.
10. What are the practical difficulties in the way of International Bimetallism ?
11. Enumerate the chief effects of the introduction of the Currency and Bank Notes Act, 1928.
12. Write brief notes on the following: (a) Gold Bullion standard; (b) the Tripartite Agreement; (c) the Currency and Bank Notes Act, 1939.



## CHAPTER XLIII

### MEANS OF PAYMENT

THE remittance of money can be effected by means of coin, cheques, stamps, money orders, bank notes, bills of exchange, promissory notes, etc. As the media through which payments are made, it will be convenient to deal with the following in the order shown on diagram on page 498.

1. The Bank of England.
2. The Mint.
3. The Post Office.
4. Joint Stock Banks.

(1) **BANK OF ENGLAND.**—This institution is responsible for the issue of Bank Notes. These are promissory notes issued by a bank payable to bearer on demand. Notes issued by the Bank of England are called *Bank Notes*, whilst those issued by Scottish and Irish banks are usually referred to as *Country Notes*. The former are legal tender for any amount, even by the Bank or its branches; that is, they are exactly on the same footing as coined money. Notes of Scottish and Irish banks are not legal tender, but they are good tender, if not objected to at the time of tender.

(2) **THE MINT.**—This is an establishment chiefly concerned with the making of coins. It is situated on Tower Hill, and is under the control of the Government. The work of the Mint may be divided as follows—

1. The coinage of gold presented by the Bank of England for that purpose—a function not exercised since 1914.

2. The coinage and issue of token silver and bronze pieces as they are required, from bullion purchased on account of the Government.

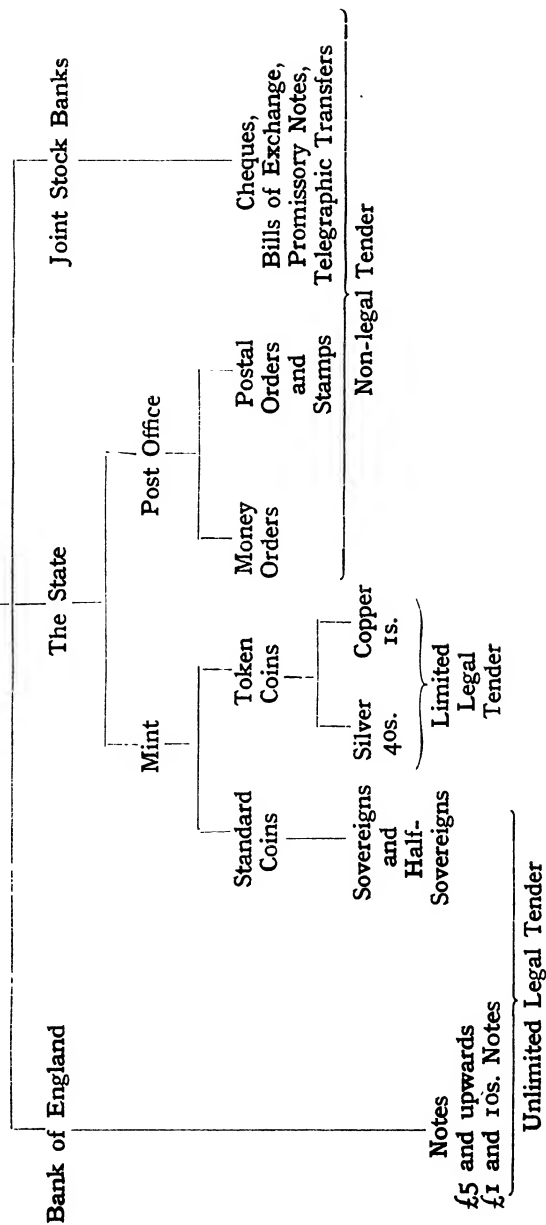
3. Execution of coinages required by British Colonies and dependencies.

4. Manufacture of naval, military, and other medals. Bronze coins are largely minted at Birmingham; and there are also Mints at Sydney and Melbourne in Australia.

In England before 1914, the coinage was said to be “free,”



# MEANS OF PAYMENT





since there were no legal impediments to prevent an individual from having his bullion coined. It was also said to be "gratuitous," since no charge was made for coinage.

In France, and some other countries, a charge is made called "seigniorage," because it was formerly paid to the seigneur or king. When the charge does not exceed the expense of minting, it is known as a "*brassage*." For instance, if it cost 1½d. to coin a sovereign, then a charge of 2d. would be a *seigniorage*, whereas 1½d. or anything less would be a *brassage*.

By the terms of the Gold Standard Act, 1925, the public could not go to the Mint with their bullion; but they sold it to the Bank of England for £3 17s. 9d. per ounce, which was the Bank price of gold, and the Bank then sold it to the Mint as required for £3 17s. 10½d. per ounce; this is known as the *Mint Price* of Gold. Gold has not been used for internal circulation since 1914.

Bullion (i.e. gold or silver in bars) has been used as international medium of settlement when other methods of payment were not available or were more expensive. These transactions were undertaken by the banks. Since 1931, however, dealings in gold have mainly been the concern of governments. Stocks of the metal have been held by Exchange Funds and Central Banks between which movements have taken place. Since the outbreak of the present war, the world's gold supplies have tended to become concentrated in the United States.

(3) **THE POST OFFICE.**—With regard to the transmission of money through the agency of the Post Office, this may be effected by the purchase of—

- |                        |                          |
|------------------------|--------------------------|
| 1. Stamps.             | 3. Inland Money Orders.  |
| 2. Postal Orders.      | 4. Foreign Money Orders. |
| 5. Registered Letters. |                          |

**Stamps.** For amounts up to 1s., remittances are often made by means of postage stamps; but for larger amounts, postal orders and money orders are used for places within the United Kingdom and many places abroad.

**Postal Orders.** These are issued at all money order offices, and many of the smaller offices which are not money order offices in the United Kingdom, during the hours in which the office is open for the sale of stamps. Postal orders can be obtained for 6d.



and for many multiples of 6d. up to 21s. Intermediate amounts may be made up by affixing postage stamps not exceeding two in number.

The sender of a postal order must fill in the name of the person to whom it is sent ; and if he so wishes, he can also fill in the name of any particular post office, when the order will be cashed at that office and no other. The insertion of the name of the paying office affords a safeguard against payment being made to a wrong person. A postal order may be crossed like a money order or a cheque. The sender should tear off and retain the counterfoil, as its production will facilitate inquiry if the order should be lost.

**Inland Money Orders.** An inland money order may be obtained for any sum not comprising a fractional part of a penny, up to £40 ; for transmission abroad, the maximum limits vary from £10 to £40. If payable in the United Kingdom, an order may be crossed through a bank. Orders for payment of sums up to £40 may also be transmitted by telegraph to offices within the United Kingdom.

The rates of poundage on ordinary inland money orders are—

For sums not exceeding £3	.	.	.	.	4d.
„ „ above £3 and not exceeding £10	.	.	.	.	6d.
„ „ „ £10	„	„	£20	.	8d.
„ „ „ £20	„	„	£30	.	10d.
„ „ „ £30	„	„	£40	.	1s.

**Foreign and Colonial Money Orders**, both ordinary and telegraphic, are also issued for transmission to and payment in almost all the British Colonies and in foreign countries. For further particulars upon this subject, the student is recommended to obtain the *Post Office Guide*, which is issued quarterly, and which contains a mass of information of great use to the business man.

(4) **JOINT STOCK BANKS.**—The economic significance of banks is based upon the fact that they are the chief medium through which payments are made and credit is brought into existence. By their agency, the money and available capital in a community are collected and then directed into the produce channels of industry. The primary function fulfilled by banks, however, is the regulation and simplification of the whole system by which payments are made and debts are settled. This is effected by the use of the following—

**Cheques.** These have come into use in consequence of the



development of the deposit business, and are orders to pay to the depositors or their order; whilst bank notes are promises on the part of the banker to pay to the bearer. The vast majority of accounts are paid by means of cheques.

**Bills of Exchange.** These are the chief means of settling international indebtedness. The use of these instruments varies somewhat with the different markets. In the East Indian trade, the terms of payment are—

1. D/P = Documents against payment at sight, 30 days' sight, 60 days' sight, and 90 days' sight.

2. D/A = Documents against acceptance at 30 days' sight, 60 days' sight, and 90 days' sight.

For trade in the more important lines, such as hardware, cotton piece goods, etc., payment is made D/P in the currency of Madras, Bombay, and Colombo.

It may appear singular that payment against documents is made at 30, 60, and 90 days' sight. In such cases, the goods are cleared by the bankers through the Customs, and are then placed in a "go-down" or warehouse, where they are stored until they are required for use. The customer has the right during the ninety days of taking up the goods against payment of the bill of exchange and the charges. When the terms are D/A, the charges are naturally avoided.

**Traders' Payments.** Under this scheme the customer gives to the bank a list of the persons to whom he wishes payment to be made, showing the names of their bankers, the branch where the account is kept, and the amount he wishes to pay to each. A cheque is drawn covering the total amount as shown on the list. The banker then transfers these amounts to the banks named and debits the account of its customer. This system combines economy with a high degree of safety.

**Telegraphic Transfers.** Beside the accounts settled by cheques and bills of exchange, there is also a system of Telegraphic Transfers, or Cable Transfers as they are often called, which is a daily rate quoted in the money market for transferring money by cable from one country to another. For example, if a person in London wished to pay a certain number of rupees to a firm in Calcutta on any particular date, he might pay into a London bank the equivalent sum of English money, calculated at the transfer rate



of the day, when the bank would cable out to their Calcutta branch to pay the nominee the sum required.

**LEGAL TENDER.**—This is any form of money which can be used as a legal quittance of a debt, and which cannot be refused by the creditor. In the British Isles, for instance, no one can be compelled to accept more than £2 in silver or one shilling in pennies or halfpennies, in satisfaction of a debt; consequently, it is said that silver is not legal tender for sums exceeding 40s. In the same way, when a sovereign is of less weight than 122·5 grains, it is no longer legal tender. The holder of such a gold coin is liable to have it clipped and rendered non-circulating, receiving in exchange for it the actual value of the gold contents.

**Token Money.** This refers to that form of money which circulates at a value given it by the Government which is higher than that of the metal contained in it. A silver shilling, if melted down, is worth less as bullion than as a coin; but a sovereign is of the exact value it purports to be. By the Coinage Act, 1920, silver coins are made of metal which consists of one-half silver and one-half alloy. Token coins are made to circulate at their nominal value by restricting their issue to meet existing needs.

**THE TREASURY.**—The Treasury is a department of the Government, and is responsible for the issue of—

1. Treasury Bills.

2. Exchequer Bonds.

**Treasury Bills** are issued in return for sums of money lent to the Government by private individuals. When the Treasury is in want of money to meet the current expenses, an advertisement is usually inserted in the *Gazette* requesting that tenders up to a certain amount be sent in to the Bank of England by a specified date; and parties having capital at their command, and being satisfied with a low rate of interest, offer to lend the Government a stated amount, and name the rate of discount they will accept. For instance, if a person offered the Treasury £100 at 4 per cent discount, he would lend only £96, but would receive a Treasury Bill for £100. The device of the Treasury Bill was originally intended to bridge seasonal discrepancies between Government revenue and expenditure, but the Great War of 1914–18 was responsible for its growth to large dimensions. In pre-war days the total issue rarely exceeded £30 million, but since the war the issue has exceeded



£900 million. The Treasury also issues Exchequer Bonds, which carry interest at a stated rate, are repayable at fixed dates, and are payable to bearer.

**Exchequer Bonds** are issued at a fixed rate of interest for a short term of years, e.g. "5 per cent Exchequer Bonds, redeemable 5th October, 1945."

Government borrowing falls under two heads—the Funded Debt, comprising permanent loans, such as Consols, and the Unfunded Debt which consists of those obligations for which a time of repayment has been stated. The Unfunded Debt includes the War Loans, some of which are repayable in a number of years, and the above-mentioned Treasury Bills and Exchequer Bonds. Owing to the magnitude of its financial operations the Treasury now exerts a considerable influence on the Money Market.

### TEST PAPER XLIII

1. Enumerate the chief media through which payments are made.
2. Copy the diagram on page 498 and name any methods of payment which are not stated thereon.
3. Explain the difference between a M.O. and a P.O. ?
4. What is the poundage on a M.O. for £4 17s. and on one for 26s. ?
5. Account for the popularity of cheques as a means of remittance as compared with bank notes.
6. Explain the use of Telegraphic Transfers.
7. Describe the chief operations which are performed by the Mint.
8. What is the meaning of Legal Tender ? Is a limitation of the legal tender of *token coins* necessary to keep up their parity value ?
9. Distinguish between Treasury Bills and Exchequer Bonds.
10. Enumerate the chief advantages and disadvantages of the use of £1 notes.
11. What are the differences between (a) a cheque, (b) a bill of exchange ? What considerations determine which shall be selected as a means of paying a debt ?
12. Explain in what respects the specialised bill of exchange, called a cheque, differs from the ordinary commercial bill of exchange.
13. You owe a customer in Glasgow £23 17s. and another in Rotterdam £145. Describe the usual methods of paying these accounts.
14. A London merchant who has no banking account wishes to send £5 10s. to a Manchester merchant in settlement of an account. By what means could he send the money ? Which means would you recommend and why ?
15. Describe briefly the facilities offered by the Post Office for the discharge of indebtedness between persons in one business centre and in another in this country. Do they possess any advantages over and above those afforded by the banks ?
16. Payment has to be made by Dawson & Co., of Manchester, to Cox & Sons, of Leicester, for a consignment of hosiery goods invoiced at £250, subject to trade discount of  $12\frac{1}{2}$  per cent and discount of  $2\frac{1}{2}$  per cent for cash. What means of payment are possible, and what is the amount involved if (a) payment is made at once ; (b) payment is delayed for six months and interest, at the rate of 5 per cent per annum is charged on all accounts running for more than three months ?



## CHAPTER XLIV

### CENTRAL BANKING

**MEANING OF THE TERM "BANK."**—The "bank" which exists by the side of a ditch is not entirely distinct in origin from the "bank" as a commercial institution. On the contrary, the original meaning of the two words was identical. A bank means something "piled up," as in the piling up of the contents of a ditch. The Teutonic word for "something 'piled up'" is *banke*, whilst the Latin word *mons* = a mound. The original meaning of the word "bank" in finance, as in agriculture, was "something piled up"; and to this day the American still speaks of making his "pile." The first meaning of the word "bank" in the commercial sense was a subscribed or piled-up loan. It was formed in the Middle Ages, when the Italian Republics were the great financial powers; and when Venice, about 1150, under the pressure of her enemies, started a subscribed loan, which, in Italian, was called *monte* and, in German, *banke*. Since Austrian-German was widely spoken in Italy at that time, the loan was known by the two names: "Monte" and "banke." The word "banke" was afterwards altered to "banco," so that "monte" and "banco" had one and the same meaning.

**IMPORTANCE OF BANKING.**—As we shall attempt to show in the course of the following chapters, banking and financial considerations are of paramount importance in the working of the economic system. Modern industry is engaged in the production of utilities for the benefit of the consumer, but as we have already seen in examining some of the many channels of distribution, producer and consumer are often widely separated both in space and in time. It is an outstanding characteristic of the modern economic system that production is undertaken in *anticipation* of demand, so that the income from the sale of goods to the consumer may not be realised for some considerable time. But the income derived from the sale of the goods represents the source from which payment is made to all those who have participated in production, and many of these cannot or are unwilling to wait until payment is received from the ultimate consumer. The electrical engineering firm which



builds generating plant for a power station in South America has to pay wages and salaries to its staff in the course of the work; it has to meet bills for material from its trade suppliers, and pay a variety of indirect expenses. Moreover, even when the equipment is complete and erected, it by no means follows that payment will be received immediately.

From this statement it will be seen that there is a gap to be bridged between the paying away of liquid resources in the form of money and the receipt of funds in payment for what has been produced. This gap may, of course, be filled from the resources of the business house itself, since, as we have seen, a certain margin of working capital (some part of which must be held in the form of cash) is indispensable. Yet it may well happen, particularly when operations are conducted upon an extensive scale, the resources of the individual business are not nearly sufficient to meet the calls which are being made upon them. Moreover in many cases, the settlement of the financial side of the transaction may be by no means straightforward as in the case of foreign trade, where differences of currencies and exchange intervene. There is obvious scope for the introduction of specialised institutions to assist in the bridging of this gap, and herein lies the function of the banking and credit system. It provides an agency for the supply of capital to business men and also a channel for the distribution of the various forms of currency utilised by the economic system of the country concerned.

The efficiency with which this task is discharged has considerable economic and social significance. As Lavington points out in his work, *The English Capital Market*: "It is evidently possible for individual producers to concentrate their energies on the output of a single kind of service or product only in so far as means are provided by which these products may be quickly and conveniently exchanged by way of purchase and sale; their specialisation is limited by the efficiency of the money system—by the ease and safety with which the community can make the payments by means of which these products are redistributed." Anything which adds to the efficiency of the banking system is therefore of direct benefit to the commercial community, whereas if the system fails to adapt itself to its economic environment, considerable injury to the whole economic structure may swiftly follow.



**NATURE OF A CENTRAL BANK.**—In view of the importance of finance in modern life, it may well be asked whether it is desirable that the provision of financial facilities should be left in the hands of private institutions. Indeed, there are many at the present time who consider that such an important function should be directly controlled by the State and who therefore demand the socialisation of the banking system. In the past, when money as a physical medium of exchange constituted the principal means of settlement of debts, the State assumed the sole rights of issue in all developed countries. Under modern conditions, however, although such State-issued money is still of importance, a far greater volume of indebtedness is settled by the use of non-legal tender currency which is created by the banks. It might therefore seem legitimate to argue that if State control is justified in the one case, it is equally necessary in the other.

Bitter experience has shown, however, that an unfettered interference of the State in currency affairs can create abuses far worse than those which it is designed to prevent. The question arises: Is it possible to evolve some system which shall confer an effective control over the financial institutions of a country and at the same time be free from political interference or the pressure of sectional interests? In most commercially developed countries the solution has been found in the creation of a specialised financial institution known as a central bank. A *Central Bank* may be defined as the principal banking institution of a country, operating under some degree of State control, and charged with the duty of regulating the volume of money and credit in the interests of the community as a whole. The objective test of the success of this policy is usually taken to be the degree of stability of value shown by the national monetary unit.

Now, the operations of an institution of this type are obviously of a special character and affect every section of the community, so that the Government cannot possibly remain indifferent to them. On the other hand, the War period revealed the great danger to the community of the State ownership of a central bank, and the Brussels Conference of 1920 came down strongly in favour of independent central banks by passing a resolution to the effect that "Banks, and especially a Bank of Issue, should be freed from political pressure and should be conducted solely on the lines of



prudent finance." Hence, most of the central banks which have been developed since the War have been treated on the lines of large public trusts regulated by the State, but not functioning under direct Government control. Yet, as a League of Nations Memorandum points out: "It is characteristic of the modern spirit that these institutions, while for the most part private or at least politically independent in their organisation, act as a bridge between the individual initiative which dominates the economic system and the public responsibilities of Governments. In so doing, they necessarily endeavour to combine the freedom characteristic of private enterprise with a sense of public responsibility."<sup>1</sup>

As a public institution charged with special responsibilities, a central bank must look further than the interests of its shareholders. In the course of its duties, not only may it have to refrain from making a profit on many of its transactions, but it may have to incur deliberate losses if it is to the public interest to do so. Again, a central bank may often have to take action in the face of public opinion and should be sufficiently strong to do so without danger of interference. Thus, the restriction of credit which may be necessary in order to curb unsound developments in boom periods will invariably provoke an outcry from the commercial world. At the same time, however, the central bank must preserve the closest contact with the needs of commerce and industry, and this may be in part secured by a judicious selection of directors. Thus, in the case of the Reserve Bank of South Africa, the charter stipulates that three directors shall be men who have been or are actively engaged in commerce and finance, one in agriculture, and two in industry. So far as the Bank of England is concerned, directors are selected on the basis of their power to bring to the Court information and knowledge as to what is proceeding in various spheres of economic activity, both in respect of domestic industry and with regard to foreign trade. No one is selected specifically as a representative of any particular industrial interest.

**FUNCTIONS OF A CENTRAL BANK.**—As already indicated, the principal responsibility of the modern central bank is, through the control of currency and credit, to maintain national economic equilibrium. From an historical standpoint, the principles of central banking were established empirically long before they received

<sup>1</sup> *World Economic Survey, 1932-1933.*



theoretical formulation. The Bank of England has been the great pioneer of central banking, but it assumed its responsibilities slowly and grudgingly. Since the War there has been a continuous development in the number of such institutions, although the scope of their authority varies greatly from one country to another. In the discharge of their basic function, central banks cannot hope to have the power to govern and direct all the factors influencing national economic equilibrium; they merely discharge an essential mediatory and regulatory function in the economic organisation. Although the precise functions of different central banks vary, the following are generally recognised as being the most essential—

(1) **Control of the Note Issue.** If the central bank is to assume responsibility for maintaining the stability of value of the national monetary unit, it must exercise the power of control over the conditions of its issue. In the majority of countries, the principal monetary unit now takes the form of a paper note which may or may not be linked with gold, so that the central bank should possess a monopoly of note issue under conditions laid down by the State. This also ensures that monetary policy shall be in some measure free from political control, for although it is competent for a Government to revise the regulations regarding note issues, this will have to be done openly, thereby giving an opportunity for an expression of public opinion in the matter. Thus the Bank of England has a monopoly of note issue in England and Wales under the Currency and Bank Notes Act, 1928, which is discussed below. Similar forms of legislation have been introduced in most economically developed countries.

(2) **Control of Gold Reserves.** In any country where the unit of money is linked with or based upon gold, the quantity of currency available to meet the internal requirements depends upon the size of the gold reserves. In consequence, in order that the available gold stock shall be employed to the best effect, it should be concentrated in the hands of the central bank. This has again been the tendency in most countries of recent years, particularly since in almost all countries gold coin has been effectively withdrawn from circulation. The result of such a concentration is to effect an economy in the use of gold and to increase the potential influences of any gold movement. All accessions of gold may be made to



exercise a maximum influence on the total volume of currency, whilst at the same time the power of central banks to influence the situation has been enhanced, as they are no longer subject to the risk that gold may be absorbed into the internal circulation. This statement still remains true to a great extent even when a country has abandoned the gold standard, provided that the currency regulations continue in force. Thus, in this country, although the Bank of England is relieved from its statutory obligation to sell gold, the provisions of the Currency and Bank Notes Act, 1928, still remain in force.

(3) **Control of Credit.** The foregoing functions are concerned mainly with the control of the legal tender currency; but, as already indicated, under modern conditions, by far the greater volume of transactions are settled by means of non-legal tender currency, mainly in the form of cheques. A cheque, in effect, operates to transfer the ownership of a certain amount of wealth in the form of a bank deposit from debtor to creditor. These bank deposits may be created either by customers who deposit funds with the bank or by the willingness of the bank itself to grant advances by way of loans or overdrafts to customers at an agreed rate of interest. The effect of these loans and overdrafts on the financial system is exactly the same as an increase in the note issue, except that they cannot be controlled directly by the Central Bank. Indirect control is obtained through the device known as the Bank Rate, which governs all other loan and interest rates in the market. Thus, if it is desired to check the extension of credit, Bank Rate is raised and all other rates of interest tend to rise in sympathy, with the result that the cost of borrowing from the banks is increased and the desire of customers to borrow is checked. This control of credit, which will be discussed more fully later, is one of the most important functions of a modern central bank.

(4) **Acting as Government Banker.** As already indicated, the relations of a central bank to the State are of a peculiar nature on account of the public importance of the functions which such a bank discharges. The ties between the central bank and the State are further strengthened by reason of the fact that it is now imperative that the bank should conduct the financial operations of the Government. The financial operations of the modern State, both on revenue and capital account, have now assumed such



dimensions that, were they conducted independently of the central bank, the resultant disturbances of credit would render its task of maintaining monetary and credit stability impossible. If, however, the control of these operations is vested in the central bank, it can take all the measures which it deems necessary to minimise their effects on ordinary business activity.

(5) **Custody of Commercial Bank Reserves.** In like manner, if the central bank is to be in a position to discharge effectively its functions of credit control, it must hold the cash reserves of the commercial bank, and these latter must be prepared to co-operate with the central bank in the enforcement of its credit policy. In certain cases, for example the United States of America, the commercial banks are required by law to keep cash reserves with the central bank equal to a certain percentage of their deposit liabilities. In England there is no such legal compulsion, but it is the custom of the commercial banks to hold cash reserves with the Bank of England of from 10 to 15 per cent of their deposit liabilities. If a fixed proportion is preserved in this way, the initiative for credit expansion is largely removed from the commercial banks and becomes vested in the central bank. In order that such a system may operate smoothly, particularly when it is on a voluntary basis, there must be close co-operation between all the institutions concerned.

(6) **Co-operation with Other Central Banks.** Matters of money and credit control are now recognised to be no longer the exclusive concern of any one country, but are of international importance. It is possible for a central bank or a Government to pursue a credit policy which will influence not only its own domestic economy, but will have far-reaching influences elsewhere. If these influences are of an adverse nature, other Governments are likely to be stirred to retaliation, often with disastrous effects on the economic life of the world. Such developments can be avoided only through co-operation between the principal banking institutions of the world. It is hoped that a medium for such co-operation will be provided by the foundation of the Bank for International Settlements at Basle, which was originally mainly concerned with the transfer problem arising out of reparations and War debts payments. It now provides a meeting-place for the world's central bankers where questions of policy may be discussed. In the monetary sphere, as in



other directions, however, international co-operation can come but slowly, for the reconciliation of divergent interests is a difficult matter.

**1. THE BANK OF ENGLAND.**—The connecting link between the Italian system of banking and modern banking is that of the goldsmiths in the seventeenth century. At that time, they were the only people who could keep valuable property safe, so that they took in the property of their customers in the form of precious metal, plate, and coin. In return for these values, they granted their customers—

(1) The right to payment in cash.

(2) The direct payment to a third person by what was called a cash loan, but what is now called a cheque.

(3) The right to a general payment from the goldsmith to pay (on demand) anybody who presented that general payment. The document was known as a goldsmith's note, and was similar to our present bank note.

During the reign of William III, when England was divided between Whigs and Tories, the country was in danger of the Stuart Pretender coming back to the throne. William III stood as the leader of the Whig party, which consisted chiefly of dissenters or Nonconformists. These Nonconformist Whigs were in danger of the Episcopalian or Roman Catholic, or Stuart, interest prevailing, for, if it had prevailed, the merchants of London—who were Whig—felt that their interests would be jeopardised. Hence, what the Government of William III most wanted were the sinews of war in the shape of money. This state of affairs led to the establishment of the Bank of England in 1694. The Bank of England was a "bank" in the original and proper sense of the word (i.e. it was a subscribed or piled-up loan of £1,200,000 engineered by a certain Scotsman named William Paterson, and was lent to the Government at 8 per cent. interest, together with £4,000 for management). These original subscribers to that loan were granted a charter, and were known by the title of the "Governors and Company of the Bank of England," and even to this day the directors are known as the "Governors" of the Bank.

Banks were afterwards started all over the country, and were in the habit of issuing large quantities of notes, although there



were many failures. In consequence of the great services rendered by the Bank of England to the Government at various times, its charter was renewed again and again.

In 1797, however, the Bank passed through its greatest crisis. It had been overstrained to finance the Great Napoleonic Wars. Pitt was continually promising not to borrow more from the Bank, but repeatedly broke his promise until, on the 25th February, 1797, the Bank of England was obliged to suspend cash payments. Owing to the depletion of the Bank's reserve on account of the assistance given to the Government, there was nothing left for it but to ask for protection. It therefore obtained from the Privy Council an order forbidding it to pay its notes in gold until further notice. This order was submitted to Parliament and confirmed, and the Bank of England was forbidden to pay its notes until further notice. This commenced the period of Bank Restriction.

**BANK RESTRICTION ACT, 1797-1819.**—The Bank Restriction Act was passed on the 3rd May, 1797, and by its terms the Bank of England was forbidden to make its payments in cash. Payment in notes was to be deemed payment in cash. The notes were to be taken at par and could be used in the payment of taxes. Notes could also be issued at a low denomination, and the Act was to remain in force for little more than a year, although it was renewed again and again.

In 1800, owing to the exchanges being very much against England, it was still considered dangerous to pay in cash—the gold being required for export. At that time it began to dawn upon many people that something must be wrong, since the market price of bullion—as measured in notes—was very much above the Mint Price. In consequence, two theories were proposed—

- (1) That the notes had declined in value ;
- (2) That the notes had risen in value.

These two theories were so greatly opposed to one another, that they were referred to a Committee of the House of Commons, which was known as the *Bullion Committee* of 1810. To that Committee was committed seven issues. They had three facts placed before them, and they were asked four questions.

1. The market price of bullion was £4 10s. per ounce.
2. Exchanges were far below par. The Paris Exchange was



14 per cent. below par (i.e. the gold sovereign would buy only 21·8892 frs. instead of 25·22 frs.).

(3) The notes were increasing and the specie was vanishing. The four questions asked were—

- (1) Are notes depreciating or appreciating ?
- (2) Has the increased issue any effect on the foreign exchange ?
- (3) What effect would a restriction of the issue have on the price of gold and on the foreign exchanges ?
- (4) How should note issues be regulated ?

Generally speaking, the Committee answered these questions by admitting the truth of the *three* facts submitted, and gave the respective replies to the questions as follows—

- (1) The notes were depreciated.
- (2) Yes ; the increased issues, when excessive, set the exchanges against us.

(3) It would raise the value of the currency, bring exchanges to par, and restore gold into circulation.

(4) The answer to this question was “ by reference to the foreign exchanges and the price of bullion.” The close watching of the movements of the foreign exchanges and the price of notes would indicate what should be done.

The Report of the Bullion Committee had to be submitted to the House of Commons. When it was moved, the resolutions were all thrown out ; and, in the presence of a price of bullion of £4 10s. per ounce, the House resolved that notes were held in public estimation as equivalent to legal coin.

Naturally, things went from bad to worse. After the rejection of the Bullion Committee Report, it was not long before the price of gold reached £5 per ounce. Then followed a serious succession of bad harvests, succeeded by good ones. The bad harvests ruined the farmers and the ruined farmers ruined the country banks, whilst these latter withdrew vast quantities of notes out of circulation. Hence, the Bank notes were no longer in excess of the people's wants, and thus recovered their value. Peel then saw his opportunity, and in 1819 he brought in the Bill for the Restoration of Cash Payments.

From 1819 to 1844 was a period of much theoretical discussion in connection with banking, being characterised by the rise of the contest between the Banking and Currency Schools. On the one



hand, the Currency doctrine, supported by Lord Overstone and other influential persons, held that it was necessary to regulate the issue of convertible notes by law; on the other hand, there was a considerable number of persons who believed in the prevailing Banking principle, and argued that, if the bank note was always convertible, its regulation could be left to the safety of the bankers, who would take care not to issue notes which they could not pay. Finally, the Currency School was triumphant, and its success was crystallised in the Bank Charter Act of 1844.

**BANK CHARTER ACT OF 1844.**—Since its foundation in 1694, gradual changes have been wrought in the constitution of the Bank of England; and it is now governed by the Bank Charter Act of 1844, whereby its various privileges were ratified and consolidated. Its five *main provisions* were—

- (1) The establishment of the Issue Department.
- (2) Anyone could take gold to the Issue Department and receive notes at the rate of £3 17s. 9d. per standard ounce.
- (3) The Bank was allowed to issue fiduciary notes to the extent of £14,000,000, on placing securities in the hands of the Issue Department. For notes issued beyond that amount, bullion or silver had to be kept by the Issue Department for a corresponding amount.
- (4) The bank note could not be issued for a smaller sum than £5.
- (5) The Bank of England was called upon to publish a weekly statement, which appears in the next succeeding *London Gazette*, and is quoted in all the chief newspapers after its issue on Thursdays.

Thus, by this Act the Issue and Banking Departments of the Bank of England were completely separated. The Issue Department could not issue any notes beyond £14,000,000 in value, unless it had an equivalent in gold or bullion for the amount of such excess. But in case a bank having the power to issue notes should relinquish the right to issue, the Issue Department of the Bank of England could increase its issue to the extent of two-thirds of the issue relinquished. Moreover, if any bank ceased to issue notes, it could not afterwards claim the right to issue; and any bank not having the right to issue notes at the time the Act was passed, could not, in the future, acquire the right to issue notes.



One of the chief purposes of the Bank Charter Act was the mitigation of crises by preventing the inflation of the currency. The Bank endeavoured to meet subsequent crises, not by the power of the Act, but by its suspension. This method, however, has proved useless. Four times the Bank Charter Act had been suspended, viz. in 1847, 1857, 1866 and 1914.

In the last-mentioned year Treasury notes were issued on the credit of Government against the taxes of the British people.

**FUNCTIONS OF THE BANK OF ENGLAND.**—The Bank of England is governed by twenty-four directors (who by long custom must not be bankers) and by a Governor and Deputy-Governor. The directors are elected annually and a part of the Court (usually the younger members) is changed every year. When a director has given several intermittent periods of service, he generally attains tenure of office for life. In due rotation he may become Deputy-Governor for two years and then Governor. But for several years past Mr. Montague Norman has held the Governorship owing to his unrivalled knowledge and wide experience. The Governor is held responsible for seeing that the securities held for investment by the Bank are of the first class. In this matter he is assisted by the Treasury Committee.

Although strictly a private undertaking, the Bank of England must be regarded as a national bank, the main function of which is to give union and direction to the flow of credit facilities. In some of its operations it resembles other national banks, such as the Bank of France and the German Reichsbank.

The actual functions of the Bank of England may be briefly stated thus—

(1) **To Manage the Note Issue.** Since 1921 the privilege of issuing notes has been withdrawn from all other banks in England and Wales. As the Bank of England enjoys the sole right of note issue, it has the power of control over the issue of the national monetary unit.

(2) **To Safeguard the Ultimate Reserve of Gold in England.** The Bank of England is responsible for the custody of the central reserve on which the integrity of the bank note is founded; in part, these reserves also form the basis on which is conducted the ordinary banking business of the country.

(3) **To Act as the Bankers' Bank.** The Bank of England has become



the depository of the cash reserves of the joint-stock banks. They are, therefore, customers of the Bank, although they receive no interest on their deposits.

(4) **To Act as a Clearing Agent.** The Bank of England acts as a clearing agent for the settlement of differences between the various banks. In this capacity it is able by mere book entries to settle the differences which arise from day to day between these banks. Unless some such arrangement existed, the banks in question would be under the necessity of holding vast sums of currency for the purpose of meeting their respective obligations to one another. Thus the Bank of England is the ultimate adjuster of debits and credits, receipts and payments, which are effected through the Clearing House.

(5) **To Conduct the Main Banking Business of the State.** The State is the collector of vast sums of money from the community in the form of taxation—Customs, Excise, Income Tax, and various other sources. All these are paid into the Government's account at the Bank of England. The Bank also looks after the payment of interest and dividends to investors in Government securities whose names are inscribed or registered in its books.

(6) **To Transact the Ordinary Business of Banking,** which may be subdivided into—

(a) The private drawing office, which keeps all accounts except those of the Government.

(b) The public drawing office, which keeps the accounts of the various departments of the State.

(c) The maintenance of branches (nine in number) for the expeditious payment of taxes to the credit of the Exchequer. These branches are established at seaport towns, such as Liverpool, Plymouth, Newcastle, Hull, and Bristol, where import duties are received.

The chief sources of profit of the Bank of England arise out of the discounting of bills, interest on loans, allowance for managing the National Debt, and profits on the note issue.

**LIMITATIONS OF THE BANK OF ENGLAND.**—There are, on the other hand, certain limitations imposed upon the Bank of England, two of which may be specially mentioned, viz.—

(1) **To Maintain Its Assets in a Liquid Form.** The liabilities of the Bank of England are all, without exception, save only such



liabilities as consist of moneys due to its own proprietors, payable on demand. It is essential, therefore, that it should maintain its assets in the most liquid form possible. Its business is to provide that the ordinary commercial trading banks of the country should have a sufficiency of credit available to form the basis of the amounts of credit that they may find it necessary to create to meet the varying demands of their customers.

(2) **To Act in the Interest of the Community as a Whole.** As a national bank, the Bank of England should not be under the necessity of having to consider whether its banking operations are to the immediate interest of its own stockholders or proprietors. It should not be under the necessity of having to assure itself of earning profits out of all the business it does. It should be free from the care of having to order its operations from the point of view of earning profit. For this reason it is usually agreed that the Bank of England should not pay interest on its deposits.

Thus the primary duty of the Bank of England is to the community as a whole. Although it has duties to the Government since it is the banker of the Government, its duties in that respect are the ordinary duties of banker to customer. Being a national bank, the Bank of England should be free from political pressure and should not be required to subordinate sound finance to the dictates of political expediency.

**THE BANK RATE.**—The Bank Rate is the official minimum rate per cent of discount charged by the Bank of England for discounting first-class bills of exchange. It is regulated by the directors at their weekly meeting, according to the quantity of gold in the market, the demand for advances, and the amount of reserve in the Bank. The movements of the Bank Rate are closely connected with the general rate of discount charged by other bankers, the explanation of which is based upon a proper understanding of the "deposit rate." For example, suppose the Bank of England were to raise its ordinary discount rate from 3 to 4 per cent. This means that other banks desirous of receiving deposits would have to offer a larger deposit rate. Since these banks would have to pay a higher rate for deposits, they therefore charge a higher rate for the amount lent to the bill-brokers. In self-defence, the bill-brokers are compelled to raise their rate of discount to the public, whose bills they negotiate. Hence the Bank of England,



by raising its discount rate, starts a rise which tends to find its way everywhere else in the country.

The primary function of the Bank Rate may be said to be the consideration of the gold reserves of the country. This result is produced on account of the secondary reactions which are set up when a rise in the rate takes place. The diagram on page 519 summarises the chief causes and consequences of changes in the Bank Rate. From this diagram it will be seen that the principal effects of a rise in the rate are generally as follows—

(1) *The Deposit Rate of the Joint-stock Banks is Increased when the Bank of England Raises its Discount Rate.* The joint-stock banks who receive money on deposit automatically raise the deposit interest rate in order that their customers may continue to maintain their deposits. If the banks did not do this, their depositors would tend to withdraw their funds and purchase first-class bills which could be discounted at an advantageous rate.

(2) *The Market Loan and Discount Rates become Dearer following on the Raising of the Deposit Rate.* The joint-stock banks have to pay more for their money, and consequently they in turn must charge a higher rate of interest for the loans they make and for discounting bills.

(3) *Credit is Restricted and Speculation Discouraged.* As the rates of interest on loans have increased, it is but natural for borrowers to make every endeavour to reduce their interest charges by reducing their loans. In order to find the money to pay off the loans, firms are compelled to allow their customers less credit than formerly, thus resulting in a general restriction of credit. Similarly, speculators often buy and sell shares with the aid of large loans from the Bank. On an increased loan rate they find that it becomes increasingly difficult to make their "turn" sufficiently large, and in consequence they liquidate the stock they may be carrying and thus there is a downward tendency in the share market.

(4) *Gilt-edged Securities become Cheaper.* The increase in the deposit rates may show that money on deposit is a more remunerative source of income than dividends and interest on Government stocks. Hence there is a tendency for the price of gilt-edged securities to fall until the yield thereon comes into line with the interest on deposits.

(5) *Prices Fall.* When money is cheap, manufacturers are often



# CAUSES AND CONSEQUENCES OF CHANGES IN THE BANK RATE

## CAUSES

- |  |         |
|--|---------|
| 1. Scarcity of money in the market.                    | Home    |
| 2. Trade boom and decrease of security.                |         |
| 3. Drain of gold to meet harvest and holiday payments. |         |
| 4. Balance of trade payments.                          | Foreign |
| 5. Efflux of gold on making payments abroad.           |         |
| 6. Fear of war and civil disturbances.                 |         |
| 1. Plentiful supply of money.                          | Home    |
| 2. Trade depression and great security.                |         |
| 3. Increased savings.                                  |         |
| 4. Balance of trade receipts.                          | Foreign |
| 5. Influx of gold on receipt of payments from abroad.  |         |
| 6. The prospects of peace and social contentment.      |         |

## Rise

## BANK RATE

## Fall

## High

## Foreign

## Home

## Low

## Foreign

## CONSEQUENCES

- |  |         |
|--|---------|
| 1. The bankers' deposit rate is increased.       | Home    |
| 2. Loan and discount rates advance.              |         |
| 3. Credit is restricted and speculation checked. |         |
| 4. Security values fall.                         |         |
| 5. General commodity prices fall.                |         |
| 6. Imports are checked and exports encouraged.   | Foreign |
| 7. Demand for trade bills on London increase.    |         |
| 8. Exchanges become favourable.                  |         |
| 9. Gold flows into the country.                  |         |
| 10. Bank reserve ultimately increased.           |         |
| 1. Money becomes more plentiful.                 | Home    |
| 2. Credit and speculation increase.              |         |
| 3. Security values rise.                         |         |
| 4. General commodity values rise.                |         |
| 5. Bankers' deposit rate falls.                  |         |
| 6. Loan and discount rates fall.                 | Foreign |
| 7. Imports increase and exports decrease.        |         |
| 8. Demand for foreign bills increases.           |         |
| 9. Exchanges become adverse.                     |         |
| 10. Gold flows out of the country.               |         |
| 11. Bank reserve ultimately falls.               |         |



in possession of large stocks which are sometimes held on credit against a bank loan. The rise of the loan rate results in an additional burden which the manufacturers find themselves unable to bear. Thus they liquidate their stocks as soon as possible, thereby causing a glut on the market and creating a fall in prices.

(6) *Imports are Discouraged and Exports Encouraged.* With the fall in prices, it will be seen that foreign markets will prove more attractive than home markets and there will be an increase in the export trade. Conversely, materials will be cheaper in England than elsewhere, and to this extent imports will decrease.

(7) *There is an Increased Demand for Short-dated Remittances and Trade Bills on London.* Following on the increase in the export trade, a greater number of foreign debtors will be buying trade bills on London for the purpose of settling their indebtedness.

(8) *Exchange Becomes Favourable.* As a result of the demand for sterling bills from foreign countries, sterling following the law of supply and demand will tend to become dearer, or, in other words, more favourable to us.

(9) *Gold may be Attracted to this Country.* The rates of exchange may become so favourable that they may rise above specie point, and then it becomes cheaper to ship gold. If gold does commence to come into the country, the Bank's gold reserve will increase, thereby allowing a larger number of notes to be put into circulation and allowing a broader basis of credit.

Converse effects would, of course, tend to follow the lowering of the Bank Rate.

**BANK OF ENGLAND RETURN.**—This return, which has been termed the "Barometer of the Money Market," is issued by the Bank every week, and gives a significant indication of the state of monetary conditions generally. The form of the return, which had remained unaltered since 1844, was changed in November, 1928, when the provisions of the Currency and Bank Notes Act, 1928, came into operation. The following brief notes explain the significance of the various items—

**Issue Department.** On the liabilities side of the Issue Department, the items are—

"*Notes Issued—in circulation, £478,448,520.*" It will be seen from the specimen return that the total amount of "Notes Issued" is £526,414,475. A glance at the assets side of the Banking



# BANK OF ENGLAND

RETURN FOR WEEK ENDED WEDNESDAY, 1st March, 1939

ISSUE DEPARTMENT		
	£	£
Notes Issued—		
In Circulation . . . . .	478,448,520	11,015,100
In Banking Department . . . . .	47,965,955	288,386,625
		12,083
		586,192
		<hr/>
Government Debt . . . . .		300,000,000
Other Government Securities . . . . .		226,414,475
Other Securities . . . . .		
Silver Coin . . . . .		
		<hr/>
Amount of Fiduciary Issue . . . . .		300,000,000
Gold Coin and Bullion (at 148s. 5d. per oz. fine)		226,414,475
	<hr/>	<hr/>
	£526,414,475	£526,414,475

BANKING DEPARTMENT		
	£	£
Proprietors' Capital . . . . .	14,553,000	99,046,164
Reserve . . . . .	3,654,252	
Public Deposits <sup>1</sup> . . . . .	11,643,224	£6,349,490
Other Deposits—		22,398,292
Bankers' . . . . .	£110,361,073	
Other Accounts . . . . .	36,549,537	
	<hr/>	<hr/>
	146,910,610	28,747,782
		47,965,955
		1,001,185
		<hr/>
	£176,761,086	£176,761,086

<sup>1</sup> Including Exchequer, Savings Banks, Commissioners of National Debt and Dividend Accounts.



Department will show that there are more than £47 million notes in the hands of the Bank itself. To find the number of notes supposed to be in circulation, it is necessary to deduct the amount held by the Banking Department from the total number actually issued as shown on the liabilities side of the Issue Department.

*"Notes Issued—In Banking Department, £47,965,955."* This item represents the actual amount of notes held by the Bank itself, as shown on the assets side of the Banking Department.

The assets held in the Issue Department against the total notes issued consist of—

*"Government Debt, £11,015,100."* This is the debt owing by the Government to the Bank, and is not represented by either stock or securities. At the original foundation of the Bank, it was stipulated that £1,200,000 should be lent to the Government, and this has gradually increased up to the above figure. The amount has remained unchanged since 1833.

*"Other Government Securities, £288,386,625."* This figure represents part of the paper "backing" behind the fiduciary issue, and in all probability consists of Treasury Bills.

*"Other Securities, £12,083."* These are all British securities, such as Commercial Bills, Consols, etc., which the Bank was permitted to hold under the provisions of the Bank Charter Act, 1844.

*"Silver Coin, £586,192."* The Bank may now hold silver coin to an amount not exceeding £5,500,000 as security for the fiduciary issue. It must be noted that this does not constitute part of the metallic backing of the note issue. The foregoing items on the assets side of the Issue Department together make up the £300 millions which represents the fixed amount of notes known as the *Fiduciary Issue* which the Bank is legally empowered to issue without a gold backing.

On the basis of the Currency and Bank Notes Act, 1928, the fiduciary issue of the Bank of England was raised from £19¼ million to £260 million and could temporarily be increased at the instance of the Bank of England with subsequent sanction by Parliament. This raising or lowering of the fiduciary issue, together with the operations of the Exchange Equalisation Account, must now be considered as forming a part of the technique of a "managed" currency. Thus, on 6th January, 1939, the Bank of England sold £200 million worth of gold to the Exchange Equalisation Account, which needed strengthening, since it had suffered heavy drains of



gold during the preceding year. The effect of the sale was to diminish the gold reserve of the Bank of England from £326 million to £126 million. In the circumstances this would have necessitated a heavy decrease in the issue of notes unless the fiduciary issue was raised. It then stood at £230 million and was forthwith increased to £400 million. The Currency and Bank Notes Act, 1939, reduced the fiduciary issue to £300 million, thus amending the Act of 1928.

*"Gold Coin and Bullion, £226,414,475."* This figure gives the amount of Gold Coin and Bullion held in the vaults of the Bank as a cash reserve against its circulation of notes. It represents virtually the whole gold reserve of the nation.

The notes issued beyond the Fiduciary Issue of £300 million are in reality Bullion Certificates, and the only way in which they can be increased in normal times is by an increase of the holdings in the Bank's vaults. There is also a line in the return for Silver Bullion, because in the Bank Act one-fifth in silver can be retained as security for the notes issued. It is a long time, however, since the Bank took advantage of this right.

**The Banking Department.** Taking the Liabilities side of the Banking Department, the items are—

*"Proprietors' Capital, £14,553,000."* This consists of the amounts which have been subscribed from time to time by the shareholders and invested in the undertaking. The original capital of the Bank was £1,200,000. Hence it will be seen there has been a considerable increase. It must be remembered that the Bank of England, although performing the functions of a central bank, is a private organisation run by its management for the benefit of its owners.

*"Rest, £3,654,252."* This item is rather a curiosity in the banking world, since it represents what the other banks call a Reserve Fund. It simply means "surplus" and, like the reserve fund of a joint-stock bank, represents an accumulation of undivided profits maintained to meet contingencies. Unlike other ordinary bank reserves, the "Rest" does not remain at a fixed level, but it fluctuates every week. It includes the balance of the Bank's profit and loss account, out of which its dividends are paid from time to time, but the total of the "Rest" is never permitted to fall below £3 million.

*"Public Deposits, £11,643,224."* This item, as is explained in the footnote to the return, represents sums standing to the credit of



various Government Departments. Among the figures contained therein are the National Exchequer Balances, Savings Banks Deposits, Deposits by the Commissioners of the National Debt, and sums held for the payment of dividends on Government and other Stocks. The figures increase very rapidly during the first half of the year, when the income and other taxes are being paid.

*"Other Deposits, £146,910,610."* This total is now separated into "Bankers" and "Other Accounts." Bankers' Balances constitute the largest part of the item and represent that portion of the cash balances of the outside banks left with the central bank. It includes the balances of the large joint-stock banks as well as the Foreign and Colonial Government balances. All the clearing bankers keep a balance with the Bank of England, which forms a kind of cash reserve, which can be drawn upon in case of need. It is interesting to note that the Bank allows no interest upon these deposits.

A rough inference may be drawn that, when the amount of "Other Deposits" is very large, money is plentiful. It implies that the joint-stock banks have a large amount of "Cash in Hand" (i.e. to their credit) at the Bank of England. The balance included among the "Other Deposits" is equivalent to cash in hand, so that it forms the first line of defence in the case of the other banks. Consequently, when the item "Other Deposits" rises above a certain level, it is expected that money will be "cheap."

On the opposite side are the Assets These are—

*"Government Securities, £99,046,164."* This includes the Bank's investments in Government Stocks and in Exchequer and Treasury Bills, in addition to its Loans to the Government on "Ways and Means Advances" and "Deficiency Bills," both of which are methods of borrowing resorted to by Government Departments to tide over temporary shortages pending the receipt of tax payments.

On the payment of dividends on the Government Stocks, warrants are issued by the Bank, and these are paid by their recipients into the various joint-stock and other banks—only to find their way again into the Bank of England as "Other Deposits."

*"Other Securities, £28,747,782."* This is separated into "Discounts and Advances" and "Securities," and represents the investments of the Bank in other than Government Securities, together with discount and loans to the money market.



When the Governors of the Bank of England come to the conclusion that money is too abundant and discount rates are too low, they decrease the amount of "Other Securities" by diminishing the amount of the securities which the Bank holds—either Government or other securities. This is effected either by selling securities or borrowing on the securities. The person making the loan to the Bank takes over the securities and, in return, pays over a cheque into the Bank of England. Under these circumstances, when the Bank borrows, there follows a decrease in the Government or "Other Securities" and also in "Other Deposits."

"Notes, £47,965,955"—"Gold and Silver Coin, £1,001,185." The total of these two amounts makes up what is known as the "Reserve" of the Bank. It is this item which is so anxiously watched in financial circles. The amount of the "Reserve" from week to week plays an important part in deciding whether the Bank will increase or reduce its rate of discount. If the Reserve in normal times *decreases* to the extent of two or three millions below the average amount, the rate will almost certainly be increased in the following week. If the Reserve is increased by such a sum above its average, the rate—if a high one—is generally reduced. A great deal depends, however, upon the period of the year, because money in the first half of the year is generally in greater abundance than it is during the second half, when the rate of discount is usually about 15s. or £1 per cent more than in the first six months of the year. It should be noticed, however, that when money is being withdrawn continuously for export, a comparatively high rate may be maintained, although the Reserve may show a considerable increase. The Bank of England always has to consider whether the amount of its holding of "Reserve" is sufficient, not only for its own liabilities, but also for the liabilities of all the other banks and for the amount of credit which is being given by the whole banking community. Thus, according to the figures in the Return set out on page 521, it will be seen that the Bank is liable in respect of Public Deposits and Other Deposits to the extent of £158,553,834; against this, the Banking Department holds Notes and Gold and Silver Coin to the value of £48,967,140. Hence it will be seen that the *proportion* of the reserve to its liabilities amounts to 30 per cent.



# **CENTRAL BANKS AND**

	<b>Bank of England</b>	<b>Federal Reserve Board</b>	<b>Bank of France</b>
<b>I. Origin</b>	Established in 1694, with a capital of £1,200,000	The Federal Reserve Act, 1913, established twelve Federal Reserve Banks under the control of a Federal Reserve Board	Established in 1800 by Napoleon Bonaparte with a capital of 30,000,000 frs. in 30,000 shares of fr. 1,000 each
<b>II. Administration</b>	There is a Governor, Deputy-Governor, and 24 other directors elected from the body of shareholders	The Board meets at Washington, and consists of the Secretary of the American Treasury, the Controller of the currency, and six other members appointed by the President of the U.S.A. with the approval of the Senate	The Governor and Deputy - Governor are appointed by the French Government, assisted by a council of 20 members
<b>III. Present capital and Reserves</b>	Present capital is £14,553,000. The Rest or Reserve Fund is never permitted to fall below £3,000,000	There is no single institution like the Bank of England. Capital and reserves are in the hands of the Federal Reserve Banks	Present capital amounts to fr. 182½ million, with reserves of over fr. 300,000,000
<b>IV. Conditions of Note Issue</b>	It has a monopoly of note issue in England and Wales. The Fiduciary issue is fixed at £300 million, beyond which a backing of gold must be kept	The Board controls the notes issued to the Reserve Banks, which must retain a gold backing of 40 per cent, which can be reduced only by permission of the Board and upon payment of interest graded according to the amount of deficiency	It has a monopoly of note issue, and must keep a reserve of gold coin and bullion worth at least 55 per cent of the combined total of notes in circulation and of the credit balance of current accounts
<b>V. Relation to the Government</b>	As banker to the Government, it manages the National Debt and attends to the issue of Government loans and to the banking operations connected with the Treasury	The most important object of the Board consists in the carrying out of a uniform national banking policy, and for this purpose it works in close co-operation with the Government	It acts as banker to the Government, issues Rentes and Treasury Bills, and discounts Bills of Exchange, but pays no interest on deposits



## THEIR CHARACTERISTICS

German Reichsbank	Commonwealth Bank of Australia	South African Reserve Bank
Established in 1876 with a capital of R.M. 120 million	Established in 1911 by a special Act of the Commonwealth Parliament	Established in 1921 by a special Act of the Union of South Africa
The Bank is independent of State control, and its administration is in the hands of three separate bodies, viz. (1) The General Council. (2) The Board of Directors. (3) The Advisory Committee	It is owned and guaranteed by the Federal Government. Its Governor and seven Directors are appointed by the Governor-General of Australia	Though a private corporation, the Government of South Africa is represented on the directorate by five out of 11 representatives. The Governor and Deputy-Governor are appointed by the Governor-General of South Africa
The capital is R.M. 150 million, divided into shares of R.M. 100 each	The nominal capital is fixed at £20,000,000	The capital of £1,000,000, subscribed by the public, may be increased with the approval of the Government. Any premium must be added to the Reserve Fund
With the exception of four minor banks, it has a monopoly of note issue. The notes must be backed by 40 per cent gold or devisen which may be reduced on payment of a graduated tax	It has a monopoly of note issue. The notes must be backed by a gold reserve of at least 25 per cent. In case of emergency, the Governor-General has power to transfer the control of the note issues to the Federal Treasury	It possesses the sole right to issue notes in the Union of South Africa. Forty per cent of its notes in circulation must be secured by gold
It makes advances to the Government and keeps the Government account; but at the end of the year the Government must not be indebted to it in any way	It is the first Government-owned bank established in the British Empire. It acts as the bank of the Commonwealth Government and also for several States	It keeps the account of the Union Government and undertakes to buy at a fixed price all the fine bullion which the producers offer to it



**II. BANK OF FRANCE.**—The Bank of France was founded in 1800 mainly through the influence of Napoleon. Since 1857 its capital has been 182½ million francs (approximately £1½ million). The term of its present charter extends till 1945. It is managed by a Governor and two Deputy-Governors, who are appointed by the President. There is a Council of twenty-three members, including the Governor and the two Deputy-Governors. Of the remaining twenty members of the Council, the Ministries of Finance, National Economy and Colonies appoint one each; six are members by virtue of their positions at the head of various Government financial departments; six are chosen by the Ministry of Finance from a list submitted by various national associations; one is nominated by the national organisation of savings banks from among its own members; one by the National Economic Council; and one by the staff of the Bank. Finally, two others, engaged in industry or commerce, but having no connection with any other bank, are elected by the shareholders. There is also a Discount Council or Committee, elected by the auditors, consisting of twelve shareholders in business in Paris. The Bank has the *monopoly of note issue*.

The Bank of France is bound to maintain a *Reserve* of 35 per cent of its total notes plus current accounts in the form of gold coin or gold bullion, subject to the provision that the remaining 65 per cent can be issued against cash, loans, or discounts.

The Bank pays no interest on current or on deposit accounts, but it discounts bills for quite small amounts, though not for a period exceeding three months. It issues letters of credit and undertakes the safe custody of securities at a charge.

The Bank acts as banker to the Government, and issues Treasury bills and bonds for the Government without charge. If the Bank Rate should go above 5 per cent, three-quarters of the profits resulting from the excess above 5 per cent go to the Government, and if the dividend exceeds a certain sum per share in any year an amount equivalent to the excess also goes to the Government.

**III. THE GERMAN REICHSBANK.**—The Reichsbank, like the Bank of England, is theoretically independent of Government control. The Bank possesses the exclusive right to issue notes subject to the existing rights that were held by four other banks. The notes are payable at the Berlin Head Office or at the branches if there is sufficient cash. The Bank can pay in gold coin, gold bars, or in



cheques payable in foreign currency based upon its gold value. The Reichsbank is obliged to maintain a *reserve* of 40 per cent. of its total notes in the form of gold or "devisen," but three-quarters of the amount must be gold. By "devisen" is meant bank notes, bills of exchange of less than fourteen days to run, cheques, and daily claims payable in foreign currency.

The proportion of the reserve may be reduced by the General Council, subject to a graduated tax ranging from 3 per cent to 8 per cent and even more if the ratio goes below  $33\frac{1}{3}$  per cent.

The Bank pays no interest on current or deposit accounts. It buys and sells gold, silver and devisen, discount bills of exchange and Treasury bills, makes loans at interest for a period not exceeding three months on the security of movable property, and takes charge of articles of value for customers.

The Bank has to undertake the general banking business of the State on special terms, but has to make no charge for acting as State banker and for managing the debt. The Bank is free from all trade, income, and corporation taxes within the Reich. A special account has to be kept for Reparation payments.

**IV. UNITED STATES FEDERAL RESERVE BANK.**—On 10th August, 1914, the Federal Reserve System of the U.S.A. supplanted the old system. Under it there are twelve Federal Reserve Banks situated in the chief banking centres of the twelve districts into which the country has been divided. All twelve are under the general control of a Committee of eight members at Washington. This Committee is known as the Federal Reserve Board. Six members, one appointed by the President of the United States, one is the Secretary of the Treasury of the United States, and the other is a Controller of the Currency of the United States. The Board acts as general manager of the entire system, but there is plenty of freedom given to the twelve banks, subject to the supervision of the Government inspectors. The most important function of the Board is the supervision of the discount rates fixed by the Reserve Banks.

**V. SOUTH AFRICAN RESERVE BANK.**—This is a central bank holding a capital of £1 million subscribed by the public. The capital may be increased by the Board of Directors with the approval of the Government, but any premium must be added to the Reserve Fund. Though it is a private corporation, the Government of South Africa is represented on the directorate by five out



of eleven representatives. The charter provides that of the six members elected by stockholders, three must be representative of commerce and finance, two of industry, and one of agriculture. The other five members, including the Governor and Deputy-Governor, are appointed by the Governor-General of South Africa. The Bank is modelled partly on the lines of the Federal Reserve Board, in so far as—

(a) Member banks are permitted to hold capital; and

(b) A share of the profits after payment of dividends goes to the State.

In the South African Bank there is provision for a cumulative dividend of 6 per cent, which may be raised to 10 per cent. Any surplus which may arise after bringing up the reserve fund to equal the share capital and providing 10 per cent for shareholders, goes to the State. In the event of liquidation, 60 per cent of the surplus assets would go to the State and 40 per cent to stock holders.

The Currency and Banking Act, 1920, made provision for the South African Reserve Bank to take over the existing issues of notes by commercial banks, so that no other authority can now issue notes without incurring the risk of stringent penalties. Specific provision is made in the Bank's statutes that no unsecured loans or drafts can be issued or real estate held except for the Bank's own operations. The member banks are required to keep as a minimum balance with the Reserve Bank 10 per cent of their demand deposits (repayable within thirty days) and 3 per cent of their time deposits. The law prohibits any interest being paid on deposits, and it also prohibits the Central Bank from taking any part in a commercial undertaking. Unlike most other central banks, it is not restricted with its investments to short-dated securities, but is permitted to deal without limit in Government securities of not more than six months' currency, but in Government securities up to two years' maturity it cannot invest a sum exceeding its paid-up capital and reserve.

**VI. COMMONWEALTH BANK OF AUSTRALIA.**—In some respects this is a Commercial and Central Bank. It is allowed by its constitution to carry on the ordinary business of banking, and yet the Commonwealth Government of Australia is responsible for all moneys due by the Bank, so that it functions as a Bank of Issue under Government guarantee.



Its nominal capital is £20 million. Of this sum, £4 million has been raised from the Reserve Fund and Redemption Fund, while a sum not exceeding £6 million can be granted to the Bank by the Government under the Commonwealth Bank Act, 1911–1925. The Bank can also raise £10 million by the issue of debentures, but none have so far been issued. Just as the Bank of England excludes from its directors any representatives of the joint-stock banks, bill-brokers, and discounters, so the Commercial Bank of Australia (like the South African Bank) disqualifies any officers of a banking institution from becoming a member of the Board.

As it is the sole note-issuing authority in Australia, heavy penalties are payable by anyone issuing notes payable to bearer on demand which might be used as currency. A separate issue department has been adopted in pursuance of the British system. The percentage of the note issue, which must be covered by gold, is unusually low at 25 per cent. Notes for 5s., 10s., £1, £5, £10, and multiples of £10 may be issued. Net profits are divided thus—

(a) One-half to the Bank Reserve Fund; and

(b) One-half to the National Debt Sinking Fund.

The weakness in its position as a central bank lies in the fact that advances and loans can be made on any securities that the Bank thinks sufficient. A central bank should only accept collateral security which is readily saleable without loss in the event of realisation, such as (a) precious metals; (b) Stock Exchange securities; (c) commercial bills payable at home; and (d) foreign currencies and bills payable abroad.

**BANK FOR INTERNATIONAL SETTLEMENTS.**—This Bank was founded in 1928 in Basle. It consists of twenty-two participants with operations in twenty-four currencies and with a staff drawn from ten different nations. There are seven founder banks, consisting of the central banks of Belgium, England, France, Germany, and Italy, the Yokohama Specie Bank of Japan, and Messrs. J. P. Morgan & Co. of the U.S.A. Shares were immediately allotted to the central banks of Sweden, Switzerland, Holland, and later to other countries. One-half of the assets and liabilities represent the foreign currency reserves of central banks; one-quarter relates to deposits of central banks for their Treasuries; the remaining quarter represents paid-in capital and permanent deposits entrusted in accordance with the Hague agreement. No deposits have yet



been accepted from private banking institutions or individuals. One average rate of interest is allowed (but the amount is not published) for all currencies on the gold or gold exchange standard. Profit-making is subordinated to the consideration of (a) a uniform central banking policy; (b) the foreign exchanges, and (c) improvement of world credit. Ten per cent only of the funds are invested for over six months and none over two years, so that great liquidity is maintained. Its aim may be said to be the super-national management of money.

Certain criticisms have been advanced against the Bank—

(1) The preponderating representation is given to the reparation Powers, so that the Bank cannot be truly international in its character.

(2) It is given power to transact business without being limited to central banks, that is, with nationals of any country, provided the central bank of that country does not object.

(3) Competitive jealousies are ceaselessly provoked.

On the whole, however, it is advantageous because the governments of central banks can meet for confidential discussion and for the exchange of methods and ideas. It is hoped the Bank will function in settling balances between the central banks of various countries in much the same way that the Bank of England functions in the final settlement of balances between English banks, without frequent heavy movements of bullion. Its future will depend largely on the extent to which it receives support from the U.S.A.

From the foregoing it will be seen that particular central Banks trace their origin to different combinations of circumstances—the necessities of public finance, a desire to foster financial or industrial development, or the desirability of establishing sound currency policies. Thus, in the case of Canada, which has recently formed a central bank for the first time, the step has been taken on the grounds that Canada has lacked a single banking authority responsible for regulating the volume of currency and credit, for maintaining the external stability of the currency and giving impartial expert advice to the Government on matters of financial policy.



## TEST PAPER XLIV

1. What is the meaning of the term "Bank"? Trace the origin of the word.
2. Classify Banks according to their legal constitution.
3. "The Bank of England was a Bank in the original and proper sense of the word." Explain this.
4. Discuss the advantages and drawbacks of a central bank. What different forms may a central banking system take?
5. What was the Bank Restriction Act of 1797?
6. What was the object of the Bullion Committee of 1810?
7. What were the conclusions arrived at by the Bullion Committee of 1810?
8. What were the main provisions of the Bank Charter Act of 1844?
9. Give, broadly, the facts respecting the note circulation in the United Kingdom since the enactment of the Charter Act (1844). What light do they afford as to the course of monetary and banking development during this period?
10. Make a copy of the Bank Return on page 521 and explain each item contained therein.
11. Explain, in detail, the items on the Assets side of the account of the Issue Department. If the Bank Charter Act is actually broken, what is the effect of this upon the figures in the Bank Return?
12. Indicate the immediate effects upon the items in the weekly statement of the Bank of England when £20 million in gold is paid out to foreigners by the Bank on behalf of the British Government.
13. Give a *pro forma* example of the Bank Return and show the effects upon that Return of the following operations considered separately—  
(a) Purchase of gold. (b) Purchase of Government Securities by the Banking Department. (c) Payment of £7,000,000 to Government Contractors. (d) Reduction of the Fiduciary Issue by £15,000,000.
14. What is the Bank Rate? How is it connected with the Deposit Rate?
15. Enumerate the chief causes of the changes in the Bank Rate of Discount.
16. Mention some of the consequences of a change in the Bank Rate.
17. State clearly the functions of the Bank of England.
18. State the character of the Liabilities of the Bank of England and the nature of its reserve. What is the special importance of the Bank Reserve?
19. The Macmillan Report states that the central bank of a country should possess four rights, viz. (a) to issue notes; (b) to hold reserves of the commercial banks; (c) to buy and sell securities; and (d) to discount bills. Explain, and enlarge on, each of these rights.
20. Does experience in Great Britain and other countries suggest that the existence of centralised banks is essential to modern banking?
21. What functions are or could be performed by the Bank for International Settlements?
22. Describe the main characteristics of the banking system either in (a) Germany, or (b) France.
23. Describe the features of the Central Bank in (a) Australia, or (b) South Africa, indicating in particular any points of strength or of weakness.
24. What do you consider to be the essential characteristics of a Central Bank? Show the relation between these characteristics and the functions which such a bank is expected to perform.
25. At the Economic Conference, 1933, recommendations were made that such Dominions as at that time did not have central banks should establish them, so that they might co-operate in future with the Bank of England and other central banks. Give some account of how far these recommendations have been carried out, and the advantages expected to be obtained from such a policy.



## CHAPTER XLV

### COMMERCIAL BANKING

**NATURE OF COMMERCIAL BANKING.**—Commercial banking may be distinguished from central banking on the grounds of the objective towards which it is directed. A commercial bank is conducted like any other business with a view to earning a maximum profit for its proprietors. It does this by rendering a variety of services acceptable to its customers with a view to increasing its connection to the greatest extent possible. A central bank, on the other hand, must take a wider view and must operate as a public institution for the benefit of the community as a whole.

Nearly all the business of the commercial banks in Great Britain is conducted by a small number of joint stock banks which have grown to their present size through a long series of amalgamations. In the nineteenth century there was a comparatively large number of banks, mostly with branches operating all over the country and in close touch with the local needs of industry and commerce. In 1913 there were forty-three joint stock banks in England and Wales, and to-day there are sixteen, of which the Big Five carry on the vast majority of the business.

**EVOLUTION OF COMMERCIAL BANKING.**—Records of money changing and advances on security are to be found in Babylonian and Assyrian inscriptions, and the ancient Greeks and Romans were acquainted with the systems of deposits bearing interest, and with letters of credit. Towards the end of the period of commercial and economic insecurity of the Middle Ages, various functions of modern banking were developed, especially on the Continent, where a system of offsetting mercantile debts arose out of the business of dealing in foreign money—a business indispensable to the traders who frequented the great mediaeval fairs. Before the year 1400, the Venetian money-changers had developed into recognised keepers of deposits, and certain prominent merchant families took the foremost place in business of this kind, arising out of the trade of Venice with the Orient.

So far as England is concerned, from the time of William the



Conqueror to the end of the thirteenth century, the chief dealers in money were the Jews, who made themselves so valuable to the Crown and to the nobility that they were usually allotted special quarters—the “Jewry”—and special protection in every walled town of importance. As a concession to popular prejudice, however, they were expelled from England by Edward I in 1290, their place being taken by the Lombards; these were money dealers with Central European and Italian connections, who received their nickname largely through being associated in the popular mind with their wealthier and more renowned brethren of Northern Italy. They are supposed to have settled in the district of Lombard Street, in the City of London. The jealousy of the City merchants led to the banishment of the Lombards by Queen Elizabeth.

In English banking there are good grounds for concluding that the scrivener was the first English pioneer. It was the custom in England during the sixteenth and early seventeenth centuries for merchants to entrust their book-keeping work to professional scriveners, who also acted as cashiers. This work gave them an intimate knowledge of financial and commercial transactions, with the result that during the seventeenth century they developed into particularly active moneylenders and recognised custodians of deposits. During the disturbed period of the Commonwealth and the Civil War, these scriveners so often proved themselves false to their trust, that the merchants began to transfer their cash reserves to the custody of the *goldsmiths*, who were a powerful factor in the economic development of England in later Stuart times. The goldsmiths began the practice of issuing receipts against the cash deposited with them, and these soon circulated better than actual coins, and may be regarded as the earliest form of bank notes issued in this country. These notes were issued against a kind of deposit account; but, in addition, the goldsmiths opened another type of account termed a “running cash,” which was the forerunner of the modern current account. The position of the goldsmiths was, however, severely shaken in 1672 by the repudiation by Charles II’s ministers of a large part of the debts of the Government. This event was of the utmost importance, as ultimately convincing the growing commercial classes that a stable banking system was a national necessity, and its influence on national thought played no small part in the foundation of the Bank of England in 1694,



from which date our modern system of banking may be said to commence.

**JOINT STOCK BANKING.**—The early history of joint stock banking in this country is very largely a story of a struggle against prejudice and vested interests. An Act passed in 1708 amending the Charter of the Bank of England prohibited the formation of banking partnerships of more than six persons. Although the Bank repudiated the suggestion that it was attempting to interfere with the goldsmith bankers, yet in virtue of this enactment, which was renewed in 1742, the Bank of England continued to function until 1826 as the only English joint stock banking company.

To meet the requirements of the Industrial Revolution, country banks in the meantime had sprung up everywhere, whilst the establishment of the London Clearing House greatly facilitated banking transactions. These small country banks, with power to issue notes and with no great financial backing, were responsible for a series of financial crises. After a particularly serious crisis in 1825, Lord Liverpool declared that the evil lay in the hundreds of small independent issues of notes of low denomination, and that these must be swept away. At the same time it had to be recognised that the Bank of England's monopoly was out of date and that some steps should be taken to improve the stability of the country banks. In order to accomplish this latter purpose, an Act was passed in 1826 permitting joint stock companies to carry on the business of banking and to issue notes at any place more than sixty-five miles from London, provided that they did not open an office within that radius. In consequence, between 1826 and the end of 1830, fourteen joint stock banks had appeared in the provinces. They were subjected to opposition from the Bank of England and from the established private bankers, whilst all kinds of misrepresentations were made to deter people from becoming either customers or shareholders. Again, in speaking of a joint stock concern at the present day, we almost invariably associate the term with limited liability. These early joint stock banking companies were, however, large partnerships with unlimited liability, and it was not until 1879 that limited liability was conferred on the banks generally.

The Bank Act of 1833 moved a step further and permitted the establishment of joint stock banking companies of more than six



## LANDMARKS IN THE EVOLUTION OF BRITISH BANKING

### 1694—FOUNDATION OF THE BANK OF ENGLAND

A Corporation formed to lend £1,200,000 at 8 per cent interest to the Government with £4,000 per annum grant for the expenses of management. This was to enable the Government of William and Mary to carry on the war with Louis XIV of France. The issue of notes was permissible up to the amount of the capital—£1,200,000.

### 1697—MONOPOLY GRANTED TO THE BANK OF ENGLAND

No other Corporation in the nature of a bank was to be established.

### 1708—BANK CHARTER RENEWED

Banks exceeding six persons were prohibited from issuing notes.

### 1720—SOUTH SEA BUBBLE

### 1797—SUSPENSION OF CASH PAYMENTS BY THE BANK OF ENGLAND

### 1810—BULLION COMMITTEE REPORT

Depreciation of notes was measured by the difference between the Mint and market prices of gold.

### 1819—CASH PAYMENTS RESUMED BY THE BANK OF ENGLAND

### 1826—BANK ACT

The right given to companies of more than six persons to issue notes when outside a radius of 65 miles from London. This created an important exception to the monopoly hitherto enjoyed by the Bank of England.

### 1833—BANK CHARTER ACT

This expressly declared that companies and partnerships, although more than six persons in number, might perform banking operations within a radius of 65 miles and even in London itself, provided they did not issue bank notes.

### 1844—BANK CHARTER ACT

This embodies the leading provisions which now govern the bank note circulation of England and Wales. The Act undertook to make the position of Bank of England Notes secure by providing for the division of the Bank into two departments—the Issue and the Banking. It also provided that the issue of notes of private banks should be strictly limited.

### 1847—BANK CHARTER ACT SUSPENDED

Financial crises also occurred in 1857, 1866, and 1914. In these years the Bank Act was again suspended; that is, the clause limiting the fiduciary issue was disregarded.

### 1857—LIMITED LIABILITY EXTENDED TO BANKS

### 1854—JOINT-STOCK BANKS ADMITTED TO THE LONDON CLEARING HOUSE

### 1914—CURRENCY AND BANK NOTES ACT

The issue of £1 and 10s. notes by the Treasury to meet the great extension of currency required to finance the Great War.

### 1920—ADOPTION OF THE "CUNLIFFE LIMIT"

### 1921—PRIVILEGE OF ISSUING NOTES FINALLY AND EXCLUSIVELY RESTRICTED TO BANK OF ENGLAND

This came about by the last of the country banks possessing the right of note issue becoming absorbed by Lloyds Bank, Ltd.

### 1925—GOLD STANDARD ACT

Export of gold re-permitted and a modified gold standard restored.

### 1928—CURRENCY AND BANK NOTES ACT

Amalgamation of Treasury notes with those of the Bank of England. The fiduciary issue of the Bank was increased from £19½ million to £260 million.

### 1931—GOLD STANDARD AMENDMENT ACT

Convertibility of bank notes suspended, with the result that Great Britain abandoned the Gold Standard.

### 1933—WORLD ECONOMIC CONFERENCE

Resolution of Empire countries in favour of the restoration of a gold standard in some modified form.

### 1934—DEVALUATION OF THE DOLLAR

### 1936—THE TRIPARTITE MONETARY AGREEMENT

### 1939—CURRENCY AND BANK NOTES ACT

The fiduciary issue of the Bank was increased to £300 million.



persons in London, provided that such corporations did not issue notes. This measure was followed by the establishment of the London and Westminster Bank in 1834 under the management of J. W. Gilbart, the London Joint Stock in 1836, the London and County in the same year, and the Union of London in 1839. A further very important step was taken in 1844, when the *Bank Charter Act* of that year provided that the note issues of the private and provincial joint stock banks were not to be increased in the future, and that the right to issue notes was to be relinquished by any such bank in the event of its bankruptcy or amalgamation.

The trend of events in English banking during the nineteenth century has been in the direction of *increasing concentration*, and most of the modern English joint stock banks have grown as the result of a long series of amalgamations. In 1825 there were more than 550 banking concerns in England and Wales, but by 1900 this number had declined to seventy-seven; whilst at the present day there are sixteen joint stock banks, of which the Big Five transact the bulk of the business. Any further amalgamations amongst the leading banks are extremely unlikely at the present time, since a fusion of any two of them would produce an institution much larger than other banks. Against such a danger there exists the protection of the Advisory Committee in Bank Amalgamations, which must report to the Treasury and the Board of Trade on any new banking fusion which is proposed. It is certain that no important banking amalgamation could be carried out in face of an adverse report by this Committee.

The past decade has seen sweeping changes in bank organisation and methods, and to-day the banks are amongst the most progressive of our great business institutions, both in the efficiency of their internal organisation and in their anxiety to provide ever-increasing services for their customers. In banking, as in most branches of economic activity, the *spread of mechanisation* has been exceptionally rapid. The mechanisation of bank accounting had already become an established fact in other countries before it was first introduced in England. In America, for example, the banks were faced with the relatively high cost of clerical labour and the enormous volume of cheques passing through their hands, and therefore applied mechanical accounting devices for the purpose of dealing with this work. Machines, such as the adding machine,



have, of course, been employed since the beginning of the century. This machine, however, has been the basis of much more pretentious mechanical methods, for from it has been evolved the *modern book-keeping machine*, which not merely lists and adds, but strikes a balance between debits and credits posted to individual accounts, and produces separate cumulative totals of all debits, credits, and balances posted in a given "run." As a result, there has been an enormous speeding up of the work, while liability to error has been greatly reduced.

**ORGANISATION OF A JOINT STOCK BANK.**—Joint stock banks are for the most part owned by quite small investors, thus differing from the private banks or merchant banks which are owned and managed almost entirely by private individuals. The shareholders delegate their powers of conducting the business of the bank to a Board of Directors, who are necessarily shareholders. The only direct control of the shareholders is at the annual meeting, where criticism is made and voting for re-election or rejection of directors takes place. The actual daily administration of joint stock banks is concentrated in the hands of the managing director or General Manager at Head Office. Internal control is secured over the accounts through the *auditors* and their report.

**Administrative Departments.** The services rendered by a joint stock bank are of a multifarious nature. In addition to the control of a network of branches, it falls to the lot of the Head Office staff to conduct an ordinary banking business similar to that which is carried on at the branches. As in other undertakings, the activities of the staff may be divided into administrative and executive. The General Manager and his assistants have charge of the administrative work, which is concerned with the preparation and planning of the business transactions in readiness for their execution. The determination of the nature and extent of the operations, the supervision of the liquidity and safety of the assets, and the efficiency of the various branches of work undertaken by the bank fall upon the shoulders of the General Manager, assisted by his staff.

In small branch banks these administrative duties devolve directly upon the Manager himself; but in the large branches, and especially at Head Office, special departments have to be formed.

*The Secretariat* conducts the propaganda and opens up new business connections. It receives and imparts information, and



lays down the general lines on which the business should be conducted.

The *Staff Department* engages and dismisses members of the staff, fixes and pays salaries, and in many cases keeps a careful watch over the progress of each member of the clerical staff.

The *Accountant's Department* is also under the control of the General Manager. It is responsible for the efficient organisation of the undertaking, sees to the audit of the accounts, and keeps a watchful eye over the solvency of the undertaking.

The *Legal Department* attends to all the legal questions appertaining to the business, conducts lawsuits, and supervises all matters connected with the bank's litigation.

The *Credit and Loan Department*, which has control of the bank's lending operations, attends to prospective borrowers and investigates into their financial status. It regulates the granting of credit, stipulates the requisite terms and conditions, and keeps a record of the loans actually contracted.

The *Executor and Trustee Department*, as its name implies, undertakes to act as trustee and executor on behalf of customers, and also as trustee for debenture holders.

The *New Issues Department* gives advice and supervises the raising of share capital for its customers. When a person needs more capital for his business, he naturally approaches his bank for assistance. This may take the form of a bank loan, which is subsequently repaid by the customer out of the capital raised from the new issue of shares arranged by the bank.

**Executive Departments.** The *Cashiers' Department* embraces all the work which has reference to the receipt and payment of cash. In a large bank it is possible to arrange that certain cashiers pay and others receive, and a special division of the counter is made accordingly. Precautions must be taken in this department to safeguard the bank against forgeries. For this reason a strict control is kept over all cash transactions.

*Securities Department.* The principal work of this department consists in taking care of Stock Exchange securities which are the property of the bank, or of securities lodged by customers as cover for loans. In its capacity of gratuitous bailee, the bank receives customers' jewellery and other valuables for safe custody. These are placed in the strong room of the bank, which is in the care of this department.



The *Coupons and Dividends Department* devotes itself to the collection and sale of the coupons detached from securities held on behalf of customers and also to the payment of dividends.

*Stocks and Shares Department.* This is engaged in the sale and purchase of stocks and shares on behalf of customers. These transactions are effected through the medium of official brokers, who charge the bank a smaller brokerage than usual, in view of the large amount of business done.

The *Bills of Exchange Department* deals with the recording and controlling of all bills of exchange discounted by the bank for its customers. The discounting of bills by branches, their custody in the Head Office Bill Department, and their collection at maturity form an important feature of the bank's work.

The *Foreign Department* is concerned with the business of foreign exchange, foreign credits, the remittance of funds abroad, and the issuing of drafts, letters of credit, and circular notes. The transfers involved by these transactions give rise to the necessity of maintaining corresponding currency accounts with banks abroad.

These departments deal directly with the customers. Orders which come through the post are dealt with through the *Correspondence Department*, where all the written work connected with the execution of orders is carried out. Entries are made from the paying-in slips and other vouchers into the books of first entry, and then posted into the Ledger, and ultimately the figures appear in the Balance Sheet.

At the present time there is a tendency to increased mechanisation of Ledger-posting. When this transitional period has been passed and redistribution of the present staffs has been effected, the long period formerly spent on Ledger-posting will not be required; it will all be done by machine. But mechanisation can apply only to routine work; it cannot deal with banking problems which call for clear thinking, judgment, wide general knowledge of business. There probably never was a time when these higher reaches of banking offered so much scope for initiative, so many opportunities for specialisation. British banks have an extensive organisation for dealing with all types of commercial inquiries and for facilitating foreign trade. The Legal, Intelligence, Foreign, Securities, and Bill Departments of banks offer interesting and responsible work to persons with ability and initiative, and it is this



type of person who will regard mechanisation as an advantage, not a hindrance.

**FUNCTIONS OF A JOINT STOCK BANK.**—In this country, at any rate, the main function of a joint stock bank is the receipt of money from its customers, subject to their right to withdraw such money on demand by cheque. This is the usual arrangement under which current accounts are opened and conducted; but in addition to accepting large sums of money on these terms, the banker usually receives money on deposit account, undertaking to pay the customer an agreed rate of interest upon the balance outstanding in return for the right to demand from him an agreed period of notice for all withdrawals. Thus the bulk of the funds so deposited are accepted subject to seven days' notice of withdrawal and, although in practice banks rarely insist on the fulfilment of this condition, it is an important safeguard in the event of exceptional withdrawals.

Arising out of this function of accepting money from the public is that whereby the banker lends resources to approved borrowers. So far as Great Britain is concerned, advances by joint stock banks fall into two great categories—loans and overdrafts. A loan is made when a fixed sum is advanced for a definite period of time, say, three or six months. The borrower pays interest on the amount for the period in question. An overdraft is the right to borrow up to a given amount in excess of the customer's balance and, therefore, the amount overdrawn depends on the extent to which the facilities granted are actually made use of during the period for which they are available. Hence the overdraft is a much more elastic form of borrowing.

These two functions—the receipt of deposits and the advancing of loans and overdrafts—jointly constitute an economic service of the greatest importance. In performing this work the commercial banks effect two economies. By collecting and pooling small items of capital individually unimportant, they make a large stock of capital permanently available for business and other uses. As expert lenders they supply this capital to borrowers at relatively low rates. They divert resources from channels in which they cannot find effective employment to places where they can be utilised to further the productive process.

Apart, however, from this primary function of linking up lenders and borrowers of liquid capital, the modern joint stock bank



performs a host of other functions, all of which are of considerable utility to its customers and to the community generally. These functions may be summarised as follows—

(1) To gather up unused purchasing power into a common fund, and to credit customers with their respective amounts in the form of current and deposit accounts.

(2) To use this fund by granting loans.

(3) To discount bills of exchange and promissory notes.

(4) To transmit money from one place to another.

(5) To exchange one kind of currency for another, such as bullion for coin, coin for credit.

(6) To act as agents on behalf of customers by—

(a) Making payments by cheques;

(b) Collecting money due on dividend coupons and warrants;

(c) Keeping valuables in safe custody.

The functions of a joint stock bank can be better understood by the examination of the items which appear in its Balance Sheet.

**ANALYSIS OF BANK BALANCE SHEET.**—The nature of the work performed by a banker is in its more important aspects revealed by an analysis of the balance sheet. In common with that of every other business the *liabilities side* indicates the sources from which the banker derives his funds, whilst the *assets side* shows how they are employed in the business. Broadly speaking, the banker derives his capital from two sources, viz. the inside capital, which is contributed by the proprietors, and the outside capital, provided by the depositors. Taking the items in the Balance Sheet on page 545, they may be analysed as follows—

**Liabilities Side of the Balance Sheet.**

**THE CAPITAL.** This is the capital of the bank subscribed originally by the shareholders. In this case, there is four million pounds sterling paid up, which consists of shares of £50 each, of which £8 per share has been paid. This means that every shareholder, besides holding a share on which £8 has been paid, is liable to pay up another £42. This is usually done in the case of banking shares, in order to increase the confidence of the public in the bank. If the bank, unfortunately, gets into low water and cannot meet the claims of depositors, then the shareholders, at any rate, will have this huge sum to pay up, and, consequently, there will be a large sum to fall back upon.



**CURRENT AND DEPOSIT ACCOUNTS.** This represents money which the bank's customers have paid into the bank in the ordinary way of business. A Current Account can be drawn upon at any moment, so long as it is not overdrawn; whereas a Deposit Account is opened on condition that the amount paid in is not withdrawn without a certain amount of notice. On this understanding, the banker usually allows the customer a rate of interest.

**BILLS ACCEPTED.** These are bills accepted by the bank and which the bank has made itself responsible to pay on behalf of the customers of the bank who have been buying goods, and who have asked the bank to give its name to the bills. The customer undertakes to pay the banker a certain charge or commission and to put the bank in funds before the bill is presented for payment.

From this Balance Sheet it will be seen that there are people who have so believed in the bank as to *deposit* ninety-one millions of money therein, partly because it can be cared for and partly because they can get interest for it. It has *accepted bills* for seven million pounds because customers know that everybody will believe that bills accepted by this bank will be met on the due date, and these bills will be first-rate credit instruments. People have invested capital in the bank because they believed that the enterprise would be a profitable one. The *reserve* of three millions is the sum which has been set aside by the directors of the bank, during its existence, as a further protection to the shareholders and to the depositors. Their total *paid-up capital* is four millions, and they have already accumulated out of profits not less than three millions, that is, three-quarters of their paid-up capital. The banking business is enormously profitable, as a rule, because it is conducted with a comparatively small capital, together with the help of other people's money. In the case under consideration, the capital is four millions, but the amount deposited is ninety-one millions.

The capital is the sum paid in by the shareholders when originally subscribed, and the company has to account for the four millions. The Reserve Fund has been accumulated out of the profits, and, therefore, the bank has to account to the shareholders for the Reserve Fund, and it accounts for both these items by the assets which it holds (as stated on the opposite side of the Balance Sheet).



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## AS AT 31ST DECEMBER, 19..

[illegible]



**Assets Side of the Balance Sheet.** The first item on the Assets side is the CASH IN HAND AND AT THE BANK OF ENGLAND, and this is the most liquid of the bank's assets. This item represents the actual money kept as a cash reserve against the demands made by the public. It has been seen that the public has Current and Deposit Accounts amounting to ninety-one millions, and the bank thinks that sixteen millions is quite a safe proportion to keep against the possibility of being asked for that sum. The amount reserved in this manner is arrived at by past experience.

CASH IN HAND consists of Bank of England notes, and credit in the books of the Bank of England. The fact that every bank keeps a balance at the Bank of England is important, for it leads people to feel that the banking system is a single homogeneous one, with its centre as the Bank of England.

CASH AT CALL AND SHORT NOTICE means money lent, which can be quickly realised. When it is at call, the bank can call for repayment of the money advanced at any time. CASH AT SHORT NOTICE usually requires about a week's notice. This item comes next to Cash in hand, because it is peculiarly liquid. It is lent to a class of people known as bill-brokers, who are specialised dealers in bills of exchange. Some of the money is also lent to stockbrokers, who are supposed to be of high standing, and always ready and able to pay back the money when called upon.

INVESTMENTS. These are the various investments in which the bank has placed a portion of the money received from depositors, etc., and are usually of such a nature that they are easily convertible into cash in case of emergency. It will be seen that the investments stated in this Joint Stock Balance Sheet are shown in much greater detail than those in the Bank of England Return.

The item of BILLS OF EXCHANGE may be included in the investments, so that this will amount to £22,000,000.

ADVANCES ON CURRENT ACCOUNTS represents the sum lent by the bank to its customers.

LIABILITIES OF CUSTOMERS FOR ACCEPTANCES. The bank makes commission by lending its name or accepting bills on behalf of customers. In this case, it becomes liable for the amount of the acceptances. The customers, however, undertake to meet the bills at maturity, so that they are shown on the Assets side as a *contra* account.



**THE BANK PREMISES.** Unlike the Bank of England Return, upon which the premises of the Bank are treated as a Secret Reserve, those of a Joint Stock Bank usually appear as an asset in the Balance Sheet.

An analysis of the principal items appearing in the Balance Sheets of the British Joint Stock Banks for 1934 is contained in the table on page 549. In addition to the "Big Five," there are eleven other English banks, which include Martins Bank Ltd., Messrs. Glyn, Mills & Co., and Messrs. Williams Deacon & Co. Besides these joint stock banks, there are still in existence a few private banks, and the Chartered Colonial banks, whose significance lies in the facilities they afford in the financing of Colonial trade.

**SCOTCH AND IRISH BANKS.**—During the last decade the tendency towards concentration and amalgamation which characterised English banking institutions has spread to Scotland and Ireland. Of the eight Scottish joint stock banks shown in the table, four have become affiliated to the "Big Five," although they maintain their separate identity and their power to issue notes. The first of their number to take this course was the National Bank of Scotland, Ltd., which affiliated with Lloyds Bank in 1918. Later affiliations were the British Linen Bank with Barclays, the Clydesdale Bank and the North of Scotland Bank with the Midland.

In Ireland the business of banking has been conducted with extraordinary steadiness and success. Since the passing of the Bank Act, 1845, its subsequent history pursued very closely the same process of development as in England. The credit which the banks obtained by the ready acceptance of their notes brought customers to their counters, and thus the existing system, fortunate in excellent managers, was built up gradually and surely. Irish banks experienced their full share of the political troubles from 1914–1923. Apart from the institution of the frontier between Northern Ireland and the Irish Free State, which created several new problems, many branch banks suffered damage in the disturbance. Nevertheless, progress has been made, and the banks have taken their share of the work of financial reconstruction following the inauguration of the Irish Free State in 1922. The "Big Five" have also extended their activities into Ireland; for example, the Westminster Bank acquired the control of the Ulster Bank during the War.

There now remains three joint stock banks, the chief of which is



the Bank of Ireland, which occupies the same relation to the Government as the Bank of England has done in England. At the same time, through its many branches, it competes with the other two joint stock banks for all kinds of banking business.

**PRIVATE BANKS.**—Many years before the establishment of the Bank of England, an elementary form of banking was carried on by the goldsmiths in London. As they dealt in valuable metals, they were obliged to adopt special means of protecting their property. Their customers often entrusted the keeping of plate to the goldsmiths, and in course of time merchants deposited with them their spare cash for safe custody. As the money was lying idle in their safes, the goldsmiths resorted to the practice of lending a portion at interest. With the increase in this desire or opportunity of lending, the goldsmiths attracted more deposits from the public by allowing a small rate of interest upon the amounts lodged. Against these deposits, the goldsmiths issued notes as an acknowledgment of their indebtedness; and these represent the earliest form of bank notes. Sometimes, other merchants who had acquired a reputation for skill and integrity, added banking transactions to their other business.

Such business was carried on by private firms, and, in 1708, an Act was passed prohibiting a firm of more than six partners from issuing notes. This Act prevented the development of joint stock banking, because it was thought that the issue of notes was an absolutely necessary function to enable a bank to make profit.

In 1857 the permissible number of partners in a private bank was increased from six to ten, at which number it still remains.

**DIFFERENCE BETWEEN PRIVATE BANK AND JOINT STOCK BANK.**—A private bank differs from a limited joint stock company in the following points—

(1) Each member is liable to the full extent of his property for all the debts of the firm. In a joint stock bank, the shareholder is liable only for the amount which has not been paid up on the shares taken. But in the case of banks of issue the members were not entitled to limited liability in respect of note issues.

(2) Each member of a private bank can make the firm liable for any debt he may contract on its behalf. For example, if he orders goods for the firm, or accepts a bill of exchange, the firm is rendered responsible.



# COMPARATIVE STATISTICS OF BRITISH JOINT STOCK BANKS

Number of Banks	Number of Branches	Liabilities (£ Millions)			Assets (£ Millions)							
		Paid-up Capital and Reserves	Acceptances and Enclosures	Deposits	Cash in Hand and at Bank	Money at Call and Short Notice	Discounts	Investments	Advances	Premises		
English Joint Stock Banks												
Barclays	2,080	26.1	7.2	378.8	62.3	21.4	60.0	104.8	148.8	14.8		
Lloyds	1,915	23.8	42.6	365.7	53.2	23.5	56.9	104.5	133.0	50.5		
Midland	2,105	25.7	15.8	415.5	56.1	21.0	62.8	126.2	164.3	26.5		
National Provincial	1,361	17.5	6.4	289.1	43.0	18.2	48.2	78.2	111.8	13.8		
Westminster	1,072	16.8	31.8	295.8	45.0	22.7	42.1	94.5	102.8	37.4		
Total (5)	8,533	109.9	103.8	1,744.9	259.6	106.8	270.0	508.2	660.7	143.0		
Other Banks (11)	1,527	25.4	18.2	280.3	41.2	38.4	22.8	104.1	103.5	30.5		
	10,060	135.3	122.0	2,025.2	300.8	145.2	292.8	612.3	764.2	173.5		
Scottish Banks												
Eight Banks	1,826	30.9	6.3	281.7	40.9	25.7	22.0	157.7	86.3	11.1		
Northern Irish Banks												
Three Banks	260	4.7	0.1	51.2	5.7	—	19.9	25.6	7.4	0.8		



(3) The partners generally take an active part in the management of the business; and though some refrain from doing so, and become dormant or sleeping partners, they are still liable for the debts contracted by the active partners. In joint stock companies, the management is entrusted to a supreme body, such as a Board of Directors, who appoint the higher officials; and the latter, in turn, may have authority to appoint the subordinate members of the staff. The directors have very wide powers, but they cannot engage in a business totally different from the one mentioned in their memorandum of association.

The growth of private banks up to 1810 was very considerable, and in that year there were 900 such banks issuing notes. The great depression caused by the Napoleonic Wars caused an immense number of failures, and twelve million pounds' worth of notes went out of circulation.

Between 1793 and 1825, no fewer than a thousand private banks failed.

At the passing of the Bank Charter Act of 1844, 207 private banks were issuing notes to the extent of about five million sterling, and 72 joint stock banks with an authorised issue of three and a half millions, making a total of eight and a half millions. In 1914 there were only six private banks issuing notes, and three joint stock banks, the total authorised issue being £334,820.

The tendency for amalgamation among large joint stock banks and the rapid absorption of private country banks have led to the disappearance of these banks of issue. In February, 1921, the last of these note issuing banks, viz., Fox, Fowler & Co., was absorbed, so that the Bank of England has now a monopoly of note issue. Although the private note-issuing banks have disappeared, there still survive a few private deposit banks, one of which is that of Messrs. Hoare & Co., which can trace its history back to the seventeenth century, before the establishment of the Bank of England.

**MERCHANT BANKS.**—Closely allied to the joint stock banks, though not bankers in the strict sense of the term, are the merchant bankers, commonly known by the name of Accepting Houses. These firms are almost without exception of Continental origin, but the London offices have become quite English in character during



the period in which they have been established in this country. As has already been shown, the great private bankers of London built up the deposit system of banking at home, and during this period similar banking families from the Continent were gradually drawn to establish offices in London by the attraction of the great overseas trade founded by English enterprise, especially during the Napoleonic Wars. These wars ruined the Merchant Bank of Amsterdam, which had previously been the chief centre of international trade; and thus the great Merchant Banking Houses of the Continent found it worth while to transfer their international offices to London. Among these may be mentioned the houses of Rothschild and Baring, Messrs. Schroeder, and Hambros Bank, Ltd.

Merchant bankers having definite connections with special foreign countries continue to carry on a very considerable business; since the War, however, the larger joint stock banks have tended to share in any growth of foreign business, and in several instances have established foreign branches or agencies in the chief European cities.

These merchant bankers deal almost entirely with the acceptance and discounting of bills of exchange, and some of them even import and export merchandise on their own account. They also play an important part in the issue of foreign loans in England on behalf of the countries with which they are associated. It is obvious that in times of trade disturbance or economic difficulties the giving of credit abroad may be a risky or expensive proceeding, and thus there is a necessity for a class of experts who specialise in foreign credits. Most of the merchant banks have quite definite connections with those special parts of Europe in which the particular trade interests with which they are associated are situated. They make it their business to have representatives abroad whose chief function is to know all about the principal importers and exporters of the country concerned, and to watch every change in their financial circumstances. Their standing is such that their undertaking to pay over an amount by a fixed date enables the exporter or merchant readily to obtain the credit or money down, in exchange for his goods, necessary for him to maintain his trade turnover and to pay the manufacturer without having to wait until the goods have actually been sold in the country to which they have been exported.



## TEST PAPER XLV

1. Trace the development of Joint Stock Banking in England.
2. In what respect are Joint Stock Banks dealers in credit?
3. Draw up a *pro forma* Balance Sheet of a joint stock bank and examine the considerations which the directors of the bank must keep in view in determining the securities in which they must invest the bank's funds.
4. Mention some of the peculiarities of a banker's business which distinguish it from that of other commercial houses.
5. Mention some of the various forms of security against which advances may be made, and consider the merits of each from the point of view of the banker.
6. "Every bank loan and every bank purchase of securities creates a deposit, and every repayment of a bank loan, and every bank sale, destroys one." Explain this process in detail and indicate the limits to the bank power to give credit to-day in England.
7. What are the chief circumstances which should influence a banker in determining the amount of his reserve?
8. The understated items have been extracted from the accounts of a Bank. Explain, briefly, what they represent.
  - "Liabilities of Customers on Acceptances as *per contra*" (*Cr.* side of Balance Sheet).
  - "Rebate on Bills not due" (*Dr.* side of Balance Sheet).
  - "Money at Call and Short Notice" (*Cr.* side of Balance Sheet).
  - "Bills Discounted" (*Cr.* side of Balance Sheet).
9. Show clearly the difference between a private and a Joint Stock Bank.
10. Indicate the relationship of banking to other branches of commerce and, in the light of your analysis, write an account of the functions of the modern banker.
11. Put down in order, giving the exact date, five of the most important events which have occurred in the history of English banking during the last hundred years, and then describe one of the events you mention.
12. Show the relation of the modern merchant banker to British overseas trade.
13. Mention *four* different kinds of banking service or facilities which English banks are able to offer their clients. Explain briefly, in each case, how the facility is helpful to the trader.



## CHAPTER XLVI

### THE PRACTICE OF BANKING

**BANKING OPERATIONS.**—Passing more generally to the operations of a banker, it is worth noticing that the banker does not, as is commonly supposed, deal merely in money. The banker is a broker of debts, for he brings together lenders and borrowers. His advice is that of the skilled expert, so that there is no harm in calling a banker a skilled professional lender. What he lends is not money, but the unused purchasing power which comes from and is measured by the excess of production over consumption. A farmer takes his wheat to market and sells it for £1,000. In payment, he receives not a thousand sovereigns, but a piece of paper called a cheque, which he pays into his bank, and that piece of paper gives him the power to go into any shop he likes and there purchase goods to the extent of the £1,000 in exchange for similar pieces of paper. Thus, through the medium of the cheque he is enabled to exchange his wheat for other goods. Suppose of the £1,000, he spends £100 on different requirements, he still has left £900 of unused purchasing power. If the farmer has no desire to make further purchases for the next six months, the banker can, in the meantime, lend the unused purchasing power to other people.

From the science of Jurisprudence, it is seen that there is no right without a corresponding duty and no duty without a correlative right. In the business of banking, the customers have certain rights, whilst the banker has certain duties to fulfil. The principal functions of a banker are—

- (1) To issue notes (if a note-issuing bank).
- (2) To receive deposits.
- (3) To discount bills of exchange.
- (4) To negotiate loans.

**Issue of Notes.** In the early history of English banking the issue of notes was regarded as such an integral portion of the business of a banker, that it was considered futile for a person to carry on the operations of banking unless he possessed the right to issue notes.



In 1708 associations of more than six persons were forbidden to issue notes, and for many years this was regarded as a prohibition of joint stock banking, insomuch that if a company could not issue notes, it was assumed that, in consequence, it could not lend.

This state of affairs continued until 1826, when joint stock banking was permitted. At the present time, however, the function of issuing notes is of small importance in England and Wales, for the banks that formerly exercised this right have now relinquished it, and now the time has come when the only notes issued in England and Wales are those of the Bank of England.

At one time the English bank note was convertible; any person holding such a note could receive gold in return for it on presentation at the Bank of England. Under the Gold Standard Act, 1925, however, this could no longer be done with a single note, but gold bullion could be purchased from the Bank in the form of gold bars containing approximately 400 ounces troy of fine gold at the rate of £3 17s. 10½d. per ounce standard gold, and could be paid for in notes. If the Bank were unable to honour its notes, the nation would have been in a state of bankruptcy.

In 1931 Great Britain abandoned the Gold Standard and with the passing of the Gold Standard (Amendment) Act the Bank of England is no longer bound to give gold in return for its notes, not even if the value of those presented for payment is equivalent to the value of 400 ounces of fine gold. Thus, the section of the Act of 1925 relating to the sale of gold by the Bank was suspended. This is what is meant by the suspension of the Gold Standard.

**The Receipt of Deposits.** The bank receives deposits. This is very much the same as an issue of notes. It is often forgotten that for every deposit received by a bank, there is a corresponding debt due from the bank, as in the case of the issue of notes.

The difference between deposits on current account and the issue of notes is merely one of method. The note is evidence of the right, and can be transferred from hand to hand. The current account gives the customer a similar right, but is founded on an implied contract and is transferred by the drawing of a cheque. Of course, the banker may receive money on deposit, in which case the depositor consents to waive his



right to immediate withdrawal and promises to give the banker notice thereof, in return for which the customer receives a higher rate of interest.

**The Discounting of Bills.** This is one of the most profitable branches of a banker's business. A trader takes a bill, which has three months to run, to a banker, who discounts it by giving an immediate right to the payment of a smaller sum, and accepts in exchange a postponed or distant right to call for the payment of a larger amount. Suppose the bill is for £100, payable in three months, the rate of interest being 4 per cent. per annum (i.e. £1 for the period under consideration). The banker credits the customer's account with £99, and gives him the right to withdraw immediately that sum in exchange for the right to call upon the acceptor for the payment of £100 at the date of maturity.

Since the War the commercial bill has declined in importance. In the first place, the inland bill has largely disappeared and is partly accounted for by the growing integration of British industry and finance so that internal financing and the bank overdraft have taken its place. Again, a definite maturity date is frequently irksome and to the trading community more elastic arrangements are invariably welcome. In the second place, the foreign bill after the War failed completely to keep pace with the expansion of treasury bills, and since the depression has declined severely. The diminishing volume of world trade, exchange restrictions, tariffs, and quotas explain the decline.

**The Granting of Loans.** The banker lends by the simple process of entering figures in books to the customers' accounts. Suppose the bank balance of a customer stands at £490, and a loan is made to him by the banker of £500. In the Pass Book there will be entered to the credit of the customer the balance of £490, together with the advance of £500 (i.e. a total of £990), against which the customer can draw. If the banker were to dishonour a cheque for £600, he would at once be subject to legal procedure on the part of the customer for damages. If a banker lends money, it at once becomes the inalienable right of the customer to draw cheques against the loan.

The fundamental difference between the business of banking and that of the trader is to be found in the phrase "on demand."



In all probability there is no other group of business men who are instantly bankrupt if they cannot pay their debts at a moment's notice. Payment "on demand" is the essence of the banking business. Another curious fact is that no banker is solvent. Every banker lives in a chronic state of insolvency, that is to say, there is no bank in the world of which it could be said that it could repay the total property of the customers at a moment's notice. If that were the case, it would mean that the banker had invested nothing and, in consequence, was earning nothing.

However incongruous it may appear, every banker undertakes to do, on pain of instant bankruptcy, what no bank in the world could possibly do if it were asked—that is, pay all its customers in full at a moment's notice.

The banker works upon the assumption that only a certain percentage of his customers will demand payment on any particular day. He must, however, keep sufficient reserve to ensure his safety. He must lend or invest as far as is necessary to make profits, but he must go no further than is safe, or he may be rendered bankrupt. It is on account of his skill and experience that the banker is able to decide how much he must keep in reserve and in what form he must keep it.

**THE ASSETS OF A BANKER.**—The assets of a banker may be arranged in order of liquidity as follows—

- (1) **Cash in hand**, including his reserve at the Bank of England.
- (2) **Money at Call and Short Notice**, that is, money lent on the money market to brokers from day to day, and money at short notice, not including loans for longer than seven days as a rule.
- (3) **Stock Exchange Investments**. These consist of first-class investments, which could be easily sold in normal times. The month of August, 1914, was abnormal on account of the outbreak of the Great European War. Hence, a Moratorium was passed. If all the bankers had been compelled to meet their payments, their investments would not have realised sufficient to save them from bankruptcy.
- (4) **Bills of Exchange**. These are very good investments for the banker, since their date of maturity is fixed. In a sudden emergency, however, the bill of exchange does not constitute a shield, since it is not due until a certain future time and the



banker cannot get the value until the time has elapsed. In England, it is not the custom to re-discount bills of exchange, although it is done in other countries.

(5) **Loans to Customers.** These are of little use at the time when the banker is suddenly called upon to pay, for that would be the time when the customer would also be called upon.

**RELATION OF THE BANKER TO HIS CUSTOMER.**—The relation between a banker and his customer is that of debtor and creditor, but the customer is in a better position than an ordinary creditor, because he can claim repayment without notice by simply drawing a cheque; and the banker is in a worse position than an ordinary debtor, because he is called upon to repay a loan without notice; and if he fails to pay promptly, especially if a cheque has been given to a third party, he will be liable to pay damages for injury to his customer's credit. The damages are usually assessed on a liberal scale in favour of the customer. If the banker becomes insolvent, the customer can only obtain dividend from his estate like any other creditor who has supplied the banker with goods. A customer has strictly no property lying at his bankers, unless he happens to have deposited a sum of money to be kept by the banker in safe custody. He may have a considerable sum to the credit of his account, but, unless he withdraws the amount before the trustee in bankruptcy intervenes, he will stand on the same footing as a trading creditor.

The Statute of Limitations does not apply in the case of money deposited with a banker until a cheque has been drawn on the account, when it commences to operate in the case of the cheque. Neither does it operate in the case of deeds or other valuables deposited with the banker for safe custody.

A banker who accepts a deposit makes a contract with his customer. He contracts to pay as directed; and if he pays other than as directed, he is liable to the customer. If a cheque is presented to a banker with a forged signature, and paid, the general rule is that the banker suffers the loss. From this will be seen the importance of cultivating a proper signature.

If a banker pays a post-dated cheque prior to the date mentioned thereon, he cannot debit the customer's account with the amount until the actual date of the cheque is reached.

A cheque to order can be paid only to the payee or endorsee of the



cheque, but the endorsement need not be verified by the paying banker, because it is obvious that he could not know it. The banker must know the signature of his customer, but not everybody's signature. He must know that an endorsement is *prima facie* correct, although he is not expected to know that it is the handwriting of the right person.

Again, there are other relations in which a banker stands to a customer. He may receive the bonds of a customer, detach the coupons, and place the resulting interest to the customer's account. In that case, he becomes a trustee for the customer, and may not convert such bonds to his own use. If he does, he will be criminally liable. At the same time, the banker is not entirely powerless in this matter. He may acquire a banker's lien or title and, although he has no rights of sale, he has the right to detain them until any debt due by his customer to himself has been paid.

**THE BANKER AS A LENDER.**—In the banking world there are quite a considerable number of well-known rules guiding the action of bankers in the matter of making loans to customers.

Generally speaking, borrowers from bankers are of three kinds : Private persons, commercial firms, and registered companies.

**Private Persons.** The banking rules with regard to loans to private persons are—

(1) Do not discount such bills. A private person has no business with bills of exchange, and the probability is that they are accommodation bills.

(2) Remember that private incomes may cease at death : so that if a loan is made to a person whose income is a professional one, the terms should be made to include life insurance on the borrower.

**Commercial Firms.** Very frequently a commercial firm borrows, because it has urgent need of funds to maintain credit. In this case, the rules are—

(1) Ask for a balance sheet before making the loan, because in a simple *viva voce* interview the would-be borrower is apt to put a rosy construction on his circumstances, whereas actually to draw up and sign a balance sheet which is not true would be a criminal offence.

(2) Remember that a partner binds the firm. This is a rule rather in favour of lending, for, although an intending borrower



may be of doubtful repute, as a member of a particular firm he may be a most desirable one.

**A Registered Company.** The most usual case is that of lending to a registered company. In this case, the bankers' rules are—

(1) Consult the Articles of Association of the company, because they will reveal the powers possessed by the directors; and a careful inspection of the Articles of Association will ensure that the borrowing is not *ultra vires*.

(2) In the case of new companies, be careful to see the registrar's Trading Certificate, because, according to the Companies Act of 1929, the contracts of a public limited company are not binding until the company is entitled to commence business, that is until it has allotted a considerable proportion of its shares.

(3) If it is a limited company, take security for the loan, or get some of the substantial directors to accept a joint and several promissory note, which will make them really liable. Title deeds to property are often accepted as security; but, in practice, it is usual to avoid the taking of second mortgages, and to take good care that the validity of title to property mentioned in the deeds is carefully scrutinised.

**Letters of Credit.** These are instruments addressed to agents or correspondents abroad and are handed by a banker to a customer, thus enabling the latter to obtain payment for a certain sum, or of his drafts up to a certain fixed limit. A letter of credit contains specimen signatures of the holder, and payments made thereunder must be endorsed thereon and duly advised to the issuer.

Some of these instruments promise acceptance of bills of exchange by the issuers. If the promise is absolute, the credit is termed an *open or clean* credit, whereas if the acceptance is made conditional on the remittance of documents of title to goods, it is termed a *documentary credit*. Documentary and clean credits are of great importance in financing exports and imports as they protect the foreign exporter by enabling him to draw bills for the amount of his exports on a bank with a world-wide reputation, thus facilitating negotiation of the bills and ensuring payment for the goods. The home importer, who arranges the credit, generally transmits the authority to his correspondent abroad who is then enabled to purchase goods by producing the letter as evidence of due payment.



**The Northern Banking  
Company, Ltd.**

*Jan. 10, 19..*

Memorandum of Receipt of

£348 : 14 : 1

for Credit of *The Blank*

*Manufacturing Co., Ltd.*

to whom the same is to be  
accounted for.

Teller.

*Jan. 10, 19..*

*Credit The Blank Manufacturing Co., Ltd.*

**In Account with THE NORTHERN BANKING COMPANY, Ltd.**

Cheques on London and Country Banks		Cheques on Local Banks and Branches			Bank of England Notes .....	
11	7	4	1	7	1	0
5	8	2	8	19	4	0
37	8	0	20	0	0	0
					18	4
					264	4
54	3	6	30	6	5	5
					54	3
					348	14
					1	1

*Signature of person paying in.....J. Smith..... £*



A letter of credit issued by a banker and promising to accept bills drawn upon him by a merchant abroad is known as a *confirmed credit*. This helps to support the importer's credit so that the foreign exporter has more reason to expect that the bills drawn by him will be met.

**Advantages of a Banking Account.** The advantages of a banking account to a tradesman are—

- (1) His surplus cash is kept in safety.
- (2) There are greater facilities for making and receiving payments than by cash, e.g. by the use of cheques.
- (3) If he needs further capital to extend his business, he can obtain it more easily and cheaply from a banker than from anyone else.
- (4) He can increase his operations by selling his book debts to the banker in the form of bills of exchange.
- (5) By using bankers' credits he can obtain goods from foreign suppliers which would otherwise be impossible. He can sell also in perfect safety by the same means.

**OPENING AN ACCOUNT. — Letter of Introduction.** Accounts should never be opened for a stranger without an introduction from someone known to the bank, or without making inquiry either from another bank or from some other satisfactory source. Even this procedure is not an absolute protection against fraud, but it minimises the risk.

**Paying-in Slip.** An account is opened by paying in cash, cheques or bills to the credit of a customer. The amount of each sort is written on a printed slip, which consists either of a single leaf or is taken out of a book bound with counterfoils. A specimen Paying-in Slip is shown on the previous page.

The classification of the payments into notes, silver, London and country cheques, etc., facilitates the work of the bank in dealing with the various kinds of payments, and in checking the cashiers' and other accounts. The amounts paid in become the property of the bank to whom the customer has entrusted the money, subject to the condition that the bank must ~~to~~ pay on demand, which is usually made when a cheque is drawn. Such an account is known as a *Current Account*, since the customer can add to it or withdraw the whole or part of it without giving notice. As a rule, the banker gives little or no interest on such an account.

When money is lodged at interest with a banker and cannot



be withdrawn without notice being given, such an account is known as a *Deposit Account*, and must be kept separate from the Current Account.

**SIGNATURE BOOK.**—On opening a banking account, the prospective customer is required to sign a special book known as the "Signature Book," which is kept by the bank for the purpose of verifying his customers' signatures. The signature often differs from a full name by the abbreviation of the Christian names or by writing only the initials of those names. It would be safer for the customer to adopt one particular form for his permanent signature. A short name is best written in full, because the longer a name, the greater is the facility in detecting a forgery. However, a customer should be left to follow his usual practice, for any compulsion would be probably resented; and any departure from his ordinary method of signing might lead in the end to a suspicion of forgery, although the signature is perfectly genuine. The most difficult signature to forge is that which is most legibly written.

**CHEQUE BOOK.**—A book of cheque forms is supplied to the customer, and he is charged with the price of the stamps at the rate of twopence for each cheque. Customers not in business usually prefer a book of fifty or even twenty-four cheques. Large firms and companies may find it convenient to have books of 500 cheques, with four cheques on each page divided by perforations. Such cheques may also have the name of the firm or company printed on them as protection against forgery. These books

<u>John Brown, Esq.</u>									
Statement of account with LLOYDS BANK, LTD.,									
CARDIFF									
<div style="text-align: right; border: 1px solid black; border-radius: 50%; padding: 5px; display: inline-block;">             SHEET No 27           </div>									
Date	Particulars.	Payments			Receipts			Dr. or Cr.	Balance
19—									
Jan. 1	Brought Forward				300	0	0	Cr.	300 0 0
" 2	Cash . . . .				30	0	0	Cr.	330 0 0
" 4	Self . . . . .	5	0	0				Cr.	325 0 0
" 5	Jones & Co. . .	11	10	6				Cr.	313 9 6



are more convenient when a large number of cheques has to be sent out monthly in payment of accounts and, perhaps, salaries.

**PASS BOOK.**—As soon as his account is opened, the customer is furnished with a Pass Book, in which is recorded the amounts received and paid out by the banker on his behalf. This may take the form of a bound book, but quite commonly at the present time the Pass Book Statement is furnished in loose leaf form on the lines of the specimen shown on the previous page.

The Pass Book is written up by the bank and is supposed to be a statement of the customer's account. The Pass Book should be obtained from the bank frequently, in order that the customer's cash book may be verified with the bank account.

It is important to notice that the counterfoils of the cheque book above mentioned are convenient records of the cheques drawn by the customer, and are useful in checking the Pass Books. The counterfoils of the paying-in slips, when they are bound in book form, serve a similar purpose with regard to the credit side of the Pass Book.

Any error discovered by the customer must be communicated to the bank within a reasonable time, otherwise it will be assumed that the account is correct. What is a reasonable time is a question of fact and depends upon the circumstances and upon the method of doing business. A few banks send acknowledgment forms, once or twice a year, to be signed by the customer ; but, in order to save expense, the forms are sent only to customers whose debit or credit balances exceed a certain amount. This is intended as a safeguard against omissions or insertions of wrong amounts in the customer's account. It also acts as a check upon the members of the bank's staff, and was probably chiefly framed for that purpose. If the customer is credited with too much in his Pass Book, and is led to believe from the state of his account that a certain balance is due to him, the banker will be bound to honour cheques to the extent of such balance, and will be liable for damages in case of refusal. Any error may be rectified by the banker on giving notice to his customer ; and if the notice is received before any cheques are drawn against a supposed balance, the banker will incur no liability if he dishonours cheques which exceed the amount actually due by him.

**Reconciliation Statement.** Since the Pass Book shows what has been paid into the bank, and what has been paid out, the balance



of the Pass Book should equal the balance of the Cash Book. This seldom happens in practice, however, for the following reasons—

(1) Cheques may have been drawn in payment of accounts and entered in the Cash Book, but not in the Bank Pass Book, owing to their not having been presented to the bank for payment prior to the date upon which the two books are compared.

(2) Country or foreign cheques may have been paid into the bank and entered in the Cash Book, but not credited in the Pass Book, owing to their not having been cleared, i.e. owing to their value not having been received by the bank.

(3) Charges made by the bank for collecting drafts, etc., may not have been entered in the Cash Book.

In spite of the fact that the Pass Book balance may not agree with the Cash Book balance, it is possible to make up a statement explaining this divergence, called a Reconciliation Statement. This is a statement which shows the causes of the difference between the balances of the Cash Book and the Pass Book on any given date. The balance as shown by the Pass Book is set down, and the items in the two books are compared. To this balance are added all moneys paid into the bank which have not been credited by the bank at the date of striking the balance, and from the new balance is deducted all cheques drawn on the bank which have not been cleared. The new balance should then agree with the balance on the Cash Book.

The example of such a Statement is shown on page 565.

It is the usual practice for the cashier to write up, in red ink, a copy of the Reconciliation Statement in the Cash Book itself for the convenience of future reference.

**PAID CHEQUES** may be returned to the customer with the Pass Book when it is made up, and this is the more usual course in London. They may, however, be returned at the end of six or twelve months, when the balance of the account is struck between the bank and the customer.

Although the London practice is to return cheques with the Pass Book, the country banks usually retain them. The payment of bills of exchange accepted payable or domiciled at the bank is regulated by agreement. It is not customary for the banker to pay such bills without the express or general authority given by the course of dealing between them. The banker is in a more



secure position by receiving the customer's express authority, because he runs less risk of paying a forged acceptance. When bills are discounted, the amount of the bill is put to the credit of the customer, and he is charged with the discount.

If the bills have only a few days to run before they become due, they are called *short bills*; and they are simply held for collection until the due date, when the customer receives credit.

If the customer holds stocks or shares in a company, he may give authority to the secretary of the company to pay the dividends to a bank. He is thus spared the trouble of paying in the dividend warrant to the credit of his account. The bank gives a discharge to the company by endorsing the cheque for the total amount paid by the company to the various customers. The bank sends, as an acknowledgment to the customer, the counterfoil or top portion of the dividend warrant, and thus intimates that the amount has been put to the credit of the customer's account.

**CHANGES IN BANKING METHODS.**—The past fifty years have seen great changes in banking methods as well as banking structure. Perhaps the most conspicuous of these changes is shown in the far greater variety of the services rendered by the banks. Among other things may be mentioned the more efficient arrangements for the collection of coupons and dividends, and for the safe custody of securities, deeds, and other valuables; the issue of letters of credit and travellers' cheques; the greater ease in conducting foreign exchange operations owing to the concentration of demands to buy and sell foreign currency being in fewer hands; the pooling

#### RECONCILIATION STATEMENT, 31st December, 19..

	£	s.	d.	£	s.	d.
Balance as per Bank Pass Book . . . . .				205	15	5
DEDUCT Cheques drawn, but not yet presented for payment, viz.—						
Allen & Co. . . . .	101	4	8			
Brown & Co. . . . .	41	0	10			
				142	5	6
				63	9	11
Add Cheques paid in, but not cleared—						
Curtis & Son . . . . .	84	14	9			
Dewar & Co. . . . .	98	0	2			
P. Jones . . . . .	208	16	4			
				391	11	3
Balance as per Cash Book . . . . .				£455	1	2



of the knowledge and experience of many minds; the standardising of the legal procedures involved in banking; the increase of uniformity in the matter of interest allowances and charges and in the commissions and fees for services rendered; the provision of night safes; the improvement of facilities for the exercise of thrift; and services in the capacity of executor or trustee. But the most advantageous of all is the service performed through the cheque system, which in its widespread use is a product of the past half-century.

### TEST PAPER XLVI

1. What are the functions of a Banker?
2. Examine critically the nature of bank deposits. Is it true to say that "the greater part of the banks' deposits is seen to consist, not of cash paid in, but of credits borrowed"?
3. What is meant by discounting Bills of Exchange?
4. What is the fundamental difference between the business of Banking and that of ordinary trade?
5. How are the assets of a Banker arranged in order of liquidity?
6. What is the relation of the Banker to his customer?
7. What rules usually guide the Banker in making advances to his customers?
8. What formalities are necessary in opening a Banking Account?
9. What is the difference between a Deposit and a Current Account with a Bank?
10. State clearly the use of the Signature Book.
11. Explain the object of the Pass Book.
12. What are Short Bills?
13. In what way does a banking account benefit a retail trader? What other services are rendered by the banker to the retail trade?
14. Describe the information a trader would expect to find in his Bank Pass Book. If the balance of the Pass Book did not agree with that shown by his Cash Book, what steps are necessary to reconcile the two?
15. Prepare a reconciliation statement as at the 31st January last, between the Pass Book and Cash Book of Thomas Stone. The following are the particulars: Balance as per Pass Book, £420 6s. 2d. On the 29th January the following cheques were drawn: A. Brown, £25 10s. 4d.; C. Dison, £42 4s. 6d.; E. Farrer, £67 3s. 2d.; Wages, £30. Of these only the wages cheque had been presented. £130 10s. 2d. had been paid into the bank on the 31st January, but this had not been credited in the Pass Book.
16. It has been said that the British banking system provides for the transfer of capital from those having a surplus to those who can utilise it. Write an account of the means whereby the banker performs this service.
17. "Banks lend freely to credit-worthy borrowers, but they refuse to tie up their depositors' money in long-term advances." Explain and elucidate.
18. Set out the advantages which a well-established retailer may expect to enjoy from the possession of an account with a bank.
19. What do you understand by a documentary credit, and what points would you take into consideration in dealing with a request from a customer in Bristol to open a documentary credit in Bordeaux on his behalf for the import of burgundy from France?



## CHAPTER XLVII

### NEGOTIABLE INSTRUMENTS

**A NEGOTIABLE INSTRUMENT** is an instrument by delivery of which the legal right to the money secured or represented by it is transferable from one person to another.

A non-negotiable instrument is an instrument of such a kind that the legal right secured or represented by it cannot be transferred by mere delivery, but only in some other manner prescribed by law ; e.g. in the case of an ordinary debt by an assignment in writing under the provisions of the Judicature Act, 1873.

Originally, a debt could not be assigned from one person to another, that is to say, it could be sued for only by the creditor himself, but the necessities of commerce caused this rule to be relaxed. Thus, by the custom of merchants, or the Law Merchant, as it is generally called, debts secured by bills of exchange became assignable by endorsement and delivery of the bills, whilst with regard to debts not so secured, it is now provided generally by the Judicature Act, 1873, that every debt can be assigned from one person to another so as to pass and transfer—

(1) The legal right to the debt.

(2) All legal and other remedies for the debt.

(3) The right to give a good discharge for the debt without the concurrence of the assignor ; subject, however, to the following conditions, viz.—

(a) The assignment must be absolute ; that is to say, it must not be one purporting to be by way of charge only ;

(b) The assignment must be in writing under the hand of the assignor ;

(c) Express notice of the assignment in writing must have been given to the debtor ; and

(d) The assignee takes the debt subject to equities, i.e. subject to all grounds of defence which the debtor could have set up in any action which might have been brought against the assignor ; e.g. that the assignor had no title, or only a defective title.



Hence, even at the present day, in the case of an ordinary debt, that is, one which is not secured by a negotiable instrument, the assignee cannot have, and cannot give to a third person any better title to the debt assigned than the assignor had.

**CHARACTERISTICS OF NEGOTIABILITY.**—On the other hand, there are certain instruments known to the law, and called negotiable instruments, the property in which will pass like the current coin of the realm, provided they have been put into that form in which, according to the custom of the money market and merchants in England generally, they are freely transferable from one person to another by mere delivery. Hence, a negotiable instrument differs from one which is non-negotiable, but which is assignable only, in that—

(1) *A negotiable instrument passes freely from hand to hand by delivery either—*

(a) *without endorsement if it is payable to bearer ; or*

(b) *with endorsement if it is payable to order ;*

whereas a non-negotiable instrument can be transferred from one person to another only with the formalities, and subject to the conditions, prescribed by some Act of Parliament.

(2) The holder of a negotiable instrument can sue upon it in his own name without having given any kind of notice of his holding to the person liable to pay on the instrument, whereas the assignee of an ordinary debt must give notice in writing of the assignment to the debtor.

(3) The holder of a negotiable instrument is presumed to have given consideration for it. That is to say, in any action brought upon the instrument, the burden of proof lies on the defendant to show that the holder of the instrument did not give consideration for it ; whereas if the holder of a non-negotiable instrument sues upon it, the burden of proof is upon him to show affirmatively that he gave consideration for it.

(4) The holder of a negotiable instrument, provided he is a holder in due course, is not prejudiced by any want or defect of title on the part of the person from whom he took the instrument, or of previous holders of the instrument ; whereas the holder of a non-negotiable instrument takes it subject to equities, that is to say, he can have no better title to the instrument than the person from whom he received it had. Hence, if such latter

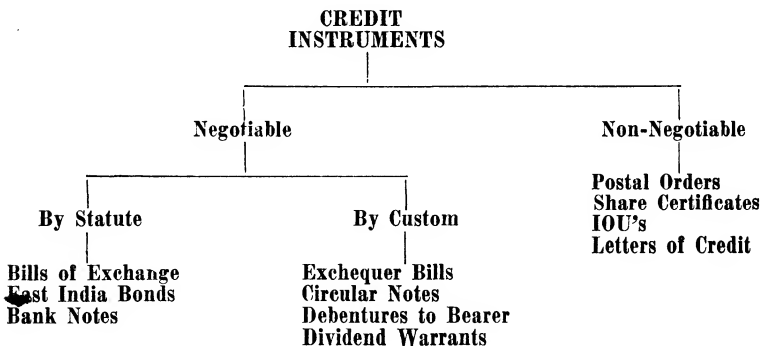


person has stolen the instrument, the holder has no title to it, and cannot give any title to a transferee of the instrument. A holder in due course of a negotiable instrument, or, as he is sometimes called, a bona fide holder for value, means a holder who has taken a negotiable instrument which is complete and regular on the face of it, in good faith and for value, and without notice at the time when the instrument was negotiated to him, of any defect in the title of the person who negotiated it.

Every holder is *prima facie* deemed to be a holder in due course, and the onus of proof is on the defendant in an action to show that the plaintiff did not take the instrument in good faith. By the Bills of Exchange Act, 1862, Section 90, "a thing is deemed to be done in good faith, within the meaning of this Act, where it is in fact done honestly, whether it is done negligently or not." Hence, in order to show that the holder of a negotiable instrument is not a bona fide holder for value, it must be proved affirmatively either—

(1) That he had actual notice of some defect of title on the part of the person who negotiated it to him ; or

(2) That he had constructive notice of some such defect in the sense that the circumstances under which he took the instrument were such as would have aroused the suspicions of any ordinary prudent man of business, and that he wilfully abstained from making such inquiries as would have disclosed to him the defect of title.



**KINDS OF NEGOTIABLE INSTRUMENTS.**—An instrument can become negotiable only in one of two ways, viz.—

(1) By the authority of an Act of Parliament ; e.g. bills of



exchange, cheques, and promissory notes under and by virtue of the Bills of Exchange Act, 1882 ; or

(2) By the universal custom of the money market and merchants in England. If an instrument is non-negotiable according to the custom of the merchants in England, it cannot be treated as negotiable in the English Courts, even though it is negotiable according to the custom of merchants where it was issued. On the other hand, a foreign instrument is not negotiable in England unless it is also negotiable in the country where it was issued, but that it is customarily transferable from hand to hand by mere delivery in England is a *prima facie* indication that it is so transferable in other countries also. The following are examples of instruments which have become negotiable by custom—

(1) Circular Notes.

(2) Dividend Warrants to bearer issued in respect of fully paid-up shares.

(3) Scrip Certificates entitling the bearer to shares in a company.

(4) Bonds or Debentures payable to holder or bearer, whether they are Government bonds or trading bonds or debentures, and whether they are foreign bonds and debentures or English ones.

On the other hand, the following instruments are not negotiable instruments in the fullest sense of the word, although they may be transferable or assignable from one person to another, viz.—

(1) Share or Stock Certificates.

(2) Debenture Stock Certificates.

(3) Share Transfers.

(4) Post Office Orders.

(5) I O U's.

(6) Bonds or Debentures not payable to holder or bearer but only to the registered holder.

In some cases, instruments are now judicially recognised as negotiable instruments, and in any legal proceedings in regard to such instruments, it is not necessary to tender evidence that they are negotiable instruments, because their negotiability is a fact of which the Court itself will take judicial notice ; e.g. the negotiability of bonds or debentures to holder or bearer has been so frequently established in various actions at law that the Court now



takes judicial notice of it. In all other cases the question whether an instrument which has never been solemnly recognised by the law is negotiable, whether it is customarily transferable by mere delivery or not, is a question of fact, which must be in each case left to the determination of the jury. If an instrument is found to be transferable by delivery according to the custom of the money market and merchants in England, the fact that such custom is of recent origin will not prevent it from being treated in law as a negotiable instrument, because the Law Merchant is not fixed, but is capable of being expanded to meet the requirements of commerce, so as to adopt from time to time those usages of merchants which are found necessary for the convenience of trade.

### TEST PAPER XLVII

1. What is meant by negotiability? What kinds of things are apt to possess this attribute and with what results?
2. What is the meaning of the term "not negotiable"? Illustrate your answer by a practical example of the application of this phrase.
3. Distinguish between a negotiable and a non-negotiable instrument.
4. Mention certain documents that are, and others that are not, negotiable in the United Kingdom.
5. Can debts be assigned? If so, under what conditions?
6. How can it be shown that the holder of a negotiable instrument is not a bona fide holder for value?
7. In what two ways can an instrument become negotiable?
8. Give four examples of instruments which have become negotiable by custom.
9. Give three examples of instruments which are not negotiable in the fullest sense of the word.
10. What is a negotiable instrument? Do all or any of the following documents come within that description—
  - (a) A Bill of Lading?
  - (b) An uncrossed cheque payable to order?
  - (c) A postal order?
11. Explain in regard to negotiable instruments the following terms—

Holder in due course.	Transferor by delivery.
Special endorsee.	Blank acceptance.
12. When does a bill which is negotiable in its origin cease to be negotiable? What is the position of a person who takes an overdue bill in settlement of a debt?
13. Distinguish between "negotiability" and "assignment," emphasising in particular the exact nature of the former, and giving examples of instruments or documents that can be regarded as negotiable.



## CHAPTER XLVIII

### BILLS OF EXCHANGE

A **BILL OF EXCHANGE** is an unconditional order in writing, addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay on demand, or at a fixed or determinable future time, a sum certain in money to, or to the order of, a specified person or to bearer.

The following is an example of a Bill of Exchange—

N <sup>o</sup> .	<u>L 25-12-6</u>	<u>August 15<sup>th</sup> 1919</u>
6d Stamp.	<u>Three months after date pay to the order</u> <u>of Henry Johnson</u>	
	<u>Twenty-five Pounds</u> <u>the sum of</u> <u>Value received</u> <u>Ten Shillings and Sixpence</u>	
	<u>To Mr. James Walker</u> <u>Bedford Street</u> <u>Cambridge.</u>	<u>John Wilson.</u>

An instrument which does not comply with these conditions, or which orders any act to be done in addition to the payment of money, is *not* a Bill of Exchange. But the sum payable by a bill is deemed to be a sum certain within the meaning of the definition, although it is required to be paid

- (a) With interest ;
- (b) By stated instalments ;
- (c) By stated instalments, with a further provision that, upon default in payment of any instalment, the whole shall become due ; or
- (d) According to an indicated rate of exchange.

Where the sum payable is expressed in words and also in figures, and there is a discrepancy between the two, the sum denoted by the words is the amount payable.



**Advantages of Bills of Exchange.** The chief advantages of a Bill of Exchange are—

(1) It fixes beyond dispute the amount owing and the time when the debt is to be paid, and affords a quicker legal remedy than an ordinary contract claim.

(2) It may be discounted, thereby enabling a party to receive the money at once, and thus “anticipate the future,” and keep his money constantly employed; whilst, on the other hand,

(3) It enables a trader to obtain the use of the goods, and affords him an opportunity of manufacturing or re-selling them, before payment becomes due; in other words, it enables him to obtain extended credit legitimately.

(4) The bill is negotiable (i.e. the debt may be assigned or transferred to another party, who may again transfer it; and so on: thus transferring value from one to another, without the actual transmission of money).

**Essentials of a Bill of Exchange.** The essentials of a Bill of Exchange are—

- |                            |                |
|----------------------------|----------------|
| (1) The date               | (4) The amount |
| (2) The period of currency | (5) The stamp  |
| (3) The parties            |                |

**DATE.** A Bill of Exchange is not invalid by reason that it is not dated. But the date may be inserted by any holder, and such date is afterwards deemed to be the true date until the contrary is proved. Nor is it invalid because it is dated on a Sunday, or is ante-dated (i.e. dated backward), or post-dated (i.e. dated forward). In calculating the due date of a bill, three days (called “Days of Grace”) are added; and if the last of these days falls on a Sunday, or on a holiday other than a bank holiday, it is payable on the preceding day; but if it falls due on a bank holiday, it is payable on the succeeding business day. But when the last day of grace is a Sunday and the second day of grace is a bank holiday, the bill is due and payable on the succeeding business day. Any alteration of the date must be confirmed by the drawer and the acceptor.

A bill may be made payable on demand, at sight, on some fixed date, or so many days or months after sight or after date. Days



of grace do not apply to bills payable on demand, at sight, or on some fixed date.

**PERIOD OF CURRENCY.** Where a bill is payable at a fixed period after date, after sight, or after the happening of a specified event, the time of payment is determined by excluding the day from which the time is to begin to run and by including the day of payment. The term "month" in a bill means a calendar month.

Where a bill is payable at a fixed period after sight, the time begins to run from the date of the acceptance if the bill is accepted.

A bill payable on demand should be presented "within a reasonable time" after it is first issued, otherwise it is deemed to be overdue, and the disabilities attaching to an overdue bill attach to it. The Bills of Exchange Act does not fix any time within which a demand bill must be presented for payment, but simply states that the facts of the particular case must determine what is a reasonable time. For example: "Pay to my order on the 12th May (fixed)," the due date of the bill would be the 12th May.

Where a bill is drawn in one country and is payable in another, the due date thereof is determined according to the law of the place where it is payable. For example, the French Code does not allow days of grace; and, therefore, a bill drawn in Paris on London is entitled to three days of grace, while a bill drawn in London on Paris is not entitled to any days of grace.

**PARTIES.** The person who gives the order to pay is called the *drawer* of the bill. The person to whom the order is given is called the *drawee*, in the first instance; and when he agrees to pay in the manner required by law—the *acceptor* of the bill; and the person in whose favour the order is given is called the *payee* of the bill. Again, the person signing his name on the back of the bill is the *endorser*, whilst the person to whom it is endorsed is the *endorsee*.

**AMOUNT.** The sum payable must be stated in words and also in figures. If there should be a difference between the two, the amount in words governs, and payment thereof can be enforced. In practice, however, it is customary to pay whichever happens to be the smaller amount.

**STAMP.** A Bill of Exchange must be drawn on stamped paper and the stamp must be an *ad valorem* impressed stamp, except



in the case of a bill or cheque payable on demand (or at sight), or three days after date or after sight, where the duty is twopence, irrespective of the amount. In the latter case, the stamp may be an adhesive one, and may be affixed by the party who draws the same, or the banker to whom it is presented for payment, and cancelled by him.

Formerly, if a bill was made payable to a particular person without the addition of the words "or order," it would not have been negotiable. But by the Bills of Exchange Act, 1882 (Sect. 8), a bill is now payable to order if it is either—

(a) Expressed to be so payable; or

(b) Expressed to be payable to a particular person, provided always that it does not contain words prohibiting transfer. On the other hand, when a bill, either originally or by endorsement, is expressed to be payable to the order of a specified person, and not to him or his order; it is nevertheless payable to him or his order at his option. When a bill contains words prohibiting transfer, it is valid as regards the parties thereto, but it is *not* negotiable.

**LOST BILLS OF EXCHANGE.**—Formerly, if a bill were lost, no action could be brought in respect of the amount payable thereon, because there was always the possibility that the bill might have got in the hands of a bona fide holder for value. But by the Bills of Exchange Act, 1882, where a bill has been lost before it is overdue, the holder may apply for another bill of the same tenor, on his giving security to indemnify the drawer in case the bill alleged to be lost is found again. If the drawee refuse to give such duplicate bill, he may be compelled to do so.

In any proceedings on a bill, the Court may order that loss of the instrument shall not be set up, provided an indemnity is given against the claims of any other person upon the instrument in question.

**PERSONS LIABLE ON A BILL.**—No person can incur liability upon a bill unless he signs it, provided—

(1) Where a person signs a bill in a trade or assumed name, he is liable thereon as if he had signed it in his own name.

(2) The signature of the name of a firm is equivalent to the signature by the person so signing of the names of all persons signing as partners in that firm.



A signature by procuration (or *per pro.*) operates as notice that the agent so signing has but a limited authority to sign, and the principal is bound by such signature only if the agent in so signing was acting within the actual limits of his authority.

On the other hand, where a person signs a bill and adds words to his signature, clearly indicating that he signs for or on behalf of a principal, or in a representative capacity, he is not personally liable thereon.

**CLASSIFICATION OF BILLS.**—A bill may be either—

- (1) An inland bill ; or
- (2) A foreign bill ;

but unless the contrary appears on the face of the bill, the holder may treat it as an inland bill.

An inland bill is one which is, or on the face of it purports to be—

- (a) Both drawn and payable within the British Islands ; or
- (b) Drawn within the British Islands upon some person resident therein.

Any other bill is a foreign bill.

**Differences between Inland and Foreign Bills.** The principal points of difference between them are—

(1) When a foreign bill is dishonoured, protest is necessary to charge any person liable on the bill other than the acceptor. In the case of an inland bill, it is optional.

(2) Foreign bills are sometimes payable at a *usage*, which means the period of time customary for payment between the two countries where the bills are drawn and are made payable, respectively. The *usage* is not applicable in the case of inland bills.

(3) An inland bill usually consists of one document only, whereas a foreign bill is sometimes drawn in a set (i.e. in two or more parts), each part of the set being numbered and containing a reference to the other parts, and the whole of the parts constituting one bill only, so that where any one part of a bill drawn in a set is discharged, the whole bill is discharged.

**Acceptance.** The acceptance of a bill is the signification by the drawee of his assent to the order of the drawer. An acceptance is invalid, unless it complies with the following conditions, viz.—

- (1) It must be written on the bill and signed by the drawee, but the mere signature of the drawee without the additional words is sufficient ; and



BILL OF EXCHANGE WITH ACCEPTANCE

Stamp



No.  \$ 

London, *EC* August 15<sup>th</sup> 99

*Ninety Days* after sight of this FIRST of Exchange  
 (second and third of the same tenor and daten) paid by pay to the  
 order of *The Velox Printing Company*

Value received

For and on behalf of  
 THE ENGLISH CARPET COMPANY, LTD.

To *The American Supply Co.*  
*5. Twenty sixth Street*  
*New York.*

*John Jones.* Director  
*S. Johnson* Secretary



(2) It must not express that the drawee will perform his promise by any other means than the payment of money.

A copy of an Acceptance is shown on page 577.

**Kinds of Acceptance.** An acceptance may be either *general* or *qualified*.

A GENERAL ACCEPTANCE assents, without qualification, to the order of the drawer.

A QUALIFIED ACCEPTANCE, in express terms, varies the effect of the bill as drawn. In particular, an acceptance is qualified which is—

(1) Conditional, i.e. makes payment by the acceptor dependent on the fulfilment of a condition therein stated—e.g. accepted payable on receipt of bills of lading.

(2) Partial, i.e. an acceptance to pay part only of the amount for which the bill is drawn.

(3) Local, i.e. an acceptance to pay only at a particular specified place. But an acceptance to pay at a particular place is a general acceptance, unless it expressly states that the bill is to be paid there only and not elsewhere.

(4) Qualified as to “time,” i.e. promising to pay at a different time from that mentioned in the bill.

(5) Qualified as to parties, i.e. where it is the acceptance of some one or more of the drawees, but not of all.

The holder of a bill has a right to require an unqualified acceptance and, if he does not obtain it, he may treat the bill as dishonoured for non-acceptance. But if he takes a qualified acceptance, and does not obtain the consent of the drawer or an endorser to the qualification, the drawer and the endorser are discharged.

A person's name may be inserted therein, to whom the holder may resort *in case of need*, i.e. if the bill is not accepted. Such a person is called “*Referee in case of need*.” But it is at the option of the holder to resort to the referee or not, as he may think fit.

(Examples of acceptances are shown on p. 579.)

**Negotiation.** A bill is negotiated when it is transferred from one person to another in such a manner as to constitute the transferee the holder of the bill. Every bill is negotiable unless it contains words showing in clear and unequivocal terms that it should not be transferred.



## EXAMPLES OF ACCEPTANCES

- |   |  |
|---|--|
| <p>(1) <i>Accepted payable at<br/>Lloyds Bank.</i></p> <p style="text-align: right;"><i>Wm. Johnson.</i></p>                        | <p>(1) General Acceptance (i.e. assents without qualification to the order of the drawer).</p>       |
| <p>(2) <i>Accepted payable on<br/>delivery of B/L at<br/>Lloyds Bank.</i></p> <p style="text-align: right;"><i>Wm. Johnson.</i></p> | <p>(2) Conditional (i.e. payment by the acceptor is dependent on the fulfilment of a condition).</p> |
| <p>(3) <i>Accepted for £90 only.</i></p> <p style="text-align: right;"><i>Wm. Johnson.</i></p>                                      | <p>(3) Partial (i.e. an acceptance to pay part only of the amount for which the bill is drawn).</p>  |
| <p>(4) <i>Accepted payable at<br/>Lloyds Bank and<br/>there only.</i></p> <p style="text-align: right;"><i>Wm. Johnson.</i></p>     | <p>(4) Local (i.e. an acceptance to pay only at a particular specified place).</p>                   |
| <p>(5) <i>Accepted payable in<br/>4 months.</i></p> <p style="text-align: right;"><i>Wm. Johnson.</i></p>                           | <p>(5) Qualified as to time, the Bill being drawn at 3 months.</p>                                   |

Nos. 2-5 are all examples of Qualified Acceptances.



A negotiable bill may be payable either—

- (1) To bearer, (2) To order.

A bill is payable to bearer—

- (a) if it is expressed to be so payable; or  
(b) if the only or last endorsement upon the bill is an endorsement in blank.

In all other cases, the bill is payable to order.

Where a bill is not payable to bearer, the payee must be named or otherwise indicated thereon with reasonable certainty. But where a payee is either—

(1) a fictitious person; (2) a non-existing person, the bill may be treated as payable to *bearer*.

A *non-existing person* means a person who has no real existence, and it is immaterial whether or not the drawer of the bill at the time when he draws the bill believes and intends the bill to be payable to the order of a real person.

A *fictitious person* means not necessarily a person who has never really existed, but a feigned or counterfeit person (i.e. a person who has not, nor was intended by the drawer to have any rights upon or arising out of the bill, so that his name may properly be said to have been used by way of pretence only).

**Endorsements.** An endorsement consists of two distinct contracts—

- (a) It transfers the property in the bill; and  
(b) it involves a liability on the part of the endorser.

A bill may be endorsed in *blank*, that is, without specifying an endorsee, and the bill then becomes payable to bearer.

A *special* endorsement specifies the person to whom, or by whose order, the bill is to be payable. The bill then becomes payable to the person designated or to his order, and can be negotiated only by his endorsement.

The endorsements are generally written on the back of the bill, but an endorsement on the face of a bill is equally valid. Examples of the different kinds of endorsements are shown on page 589.

A bill endorsed in blank may either be treated as payable to bearer, or the holder may convert the blank endorsement into a special endorsement by filling in, above the endorser's signature, a direction to pay the bill to, or to the order of, himself; or to some other person; or by inserting a special endorsement



following the endorsement in blank. A bill endorsed in blank may, therefore, circulate from hand to hand, without any further endorsement, until the blank endorsement is converted into a special endorsement.

According to law, the endorser of a bill, by the mere fact of endorsing it, guarantees the payment of the bill and also undertakes a liability in reference to its acceptance. This liability can be excluded by the use of the words "*without recourse*" or some similar words in the endorsement. The addition of these words is, however, somewhat unpopular, as they are apt to throw a doubt on the solvency of the other parties.

An endorsement must be written on the bill itself or on an "*allonge*," that is, a slip of paper attached to the bill. The first endorsement on the allonge must begin on the bill and end on the allonge, in order to prevent an allonge being taken from one bill and affixed to another.

**Presentment for Payment.** Presentment is the formal act of bringing a bill of exchange to the notice of the acceptor for payment. It must be made by the holder or by some person authorised to receive payment on his behalf, at a reasonable hour on a business day, at the proper place. A bill is presented at the proper place—

(1) Where a place of payment is specified in the bill and the bill is there presented.

(2) Where no place of payment is specified in the bill, but the address of the drawee or acceptor is given in the bill, the bill is presented there.

(3) Where no place of payment is specified and no address given, and the bill is presented at the drawee's or acceptor's place of business, if known; and if not, at his ordinary residence, if known.

(4) Where a bill is presented at the proper place, and, after the exercise of reasonable diligence no person authorised to pay or refuse payment can be found there, no further presentment to the drawee or acceptor is required.

(5) Where authorised by agreement or usage, a presentment through the Post Office is sufficient.

**DISHONOUR OF A BILL OF EXCHANGE.**—A Bill of Exchange may be dishonoured either by non-acceptance or by non-payment. Dishonour by non-acceptance takes place when the bill is duly



presented for acceptance and a proper acceptance is refused or cannot be obtained. Dishonour by non-payment takes place when the bill is duly presented for payment and payment is refused or cannot be obtained, or when presentment is excused and the bill is overdue and unpaid. A person failing to give notice of dishonour, or (in the case of a Foreign Bill) to protest the bill loses his right of recourse against drawer and endorsers.

Where the notice is given by or on behalf of the holder, it also acts for the benefit of subsequent holders and all prior endorsers who have a right of recourse against the party to whom it is given. The following is a specimen form of a Notice of Dishonour—

NOTICE OF DISHONOUR TO DRAWER

(Date and Address.)

Please take notice that a bill for £----- drawn by you under date the ----- on ----- and payable ----- has been dishonoured by non-payment (or non-acceptance).

(Signed)

J. K.

To Mr. A. B.

A Notice of Dishonour need not be in the words mentioned above; in fact, dishonour need not expressly be mentioned. Sometimes a statement that a bill is *unpaid*, and that the charges or the noting come to so much, is a good notice by implication.

**Noting a Bill.** An Inland Bill, when dishonoured, is sometimes noted, that is, presented a second time by a notary on the day of its dishonour, or not later than the next succeeding business day. If still unpaid, he affixes his note to that effect, stating the reason of its dishonour; and in a Court of law this is admitted as evidence that the bill was duly presented and dishonoured. It is not, however, imperative to note an Inland Bill, although it is generally considered desirable to do so if recourse is to be had against the drawer or endorser.

**Protesting a Bill.** A Foreign Bill must be duly protested either for non-acceptance or for non-payment. If it is not so protested, the drawer and endorsers are discharged. A *protest* means a formal notarial certificate attesting the dishonour of a bill.



## FORM OF PROTEST

UNITED STATES OF AMERICA, }  
STATE OF NEW YORK. } On the 18<sup>th</sup> day of  
September,

in the year Nineteen Hundred and     at the request  
of the holder thereof, I, THOMAS J. BROWN, a Notary  
Public of the State of New York, duly commissioned  
and sworn, did present the original Bill of Exchange  
or Cheque hereto annexed to

*Gilbert & Co.,*  
at     22 West 36<sup>th</sup> Street,     New York City,

and demanded payment thereof, which *they* refused,  
saying: *To return the draft as they would remit direct.*

WHEREUPON, I, the said Notary, at the request afore-  
said, did PROTEST, and by these presents do publicly  
and solemnly PROTEST, as well against the drawer,  
acceptor and endorsers of said Bill of Exchange or  
Cheque, as against all others whom it doth or may con-  
cern, for exchange, or re-exchange and all costs, damages  
and interest already incurred, and to be hereafter incurred,  
for want of payment of the said Bill of Exchange or  
Cheque.

THUS DONE AND PROTESTED, in the City of New York,  
aforesaid, in the presence of John Smith  
and Richard Smith, witnesses.

In Testimonium Veritatis.

Seal  
of  
Notary.

(Signed) *Thomas J. Brown,*  
NOTARY PUBLIC.



It usually contains—

- (1) An exact copy of the bill ;
- (2) A statement of the parties for whom and against whom the bill is protested ;
- (3) The place and date of the protest ;
- (4) A statement that acceptance or payment has been demanded by the notary, the answer given (if any), or a notification of the fact that no answer was given or that the drawee or acceptor could not be found ;
- (5) A reservation of rights against all the parties liable ; and
- (6) The subscription and seal of the notary.

The usual wording of the protest is found on page 583.

**ACCOMMODATION BILL.**—An Accommodation Bill is a bill which is signed by the drawer, acceptor, or endorser, without receiving value for the same, and for the purpose of lending his name to some other person. It is sometimes known as a “ fictitious bill,” a “ kite,” or a “ windmill.” So long as no value has been given for such a bill, no party is liable to pay the amount of the bill ; but directly value has been given, a holder in due course has a right to proceed against any of the signatories, even though he knows that it is an Accommodation Bill.

### TEST PAPER XLVIII

1. What is a Bill of Exchange ? Give an example.
2. Mention some of the advantages of the use of Bills of Exchange in the Home Trade.
3. Enumerate the essentials of a Bill of Exchange.
4. If a Bill of Exchange is lost, is it possible to recover the amount owing ?
5. What parties are liable on a Bill of Exchange ?
6. What is the difference between an Inland and a Foreign Bill ?
7. What is meant by “ acceptance of a Bill of Exchange ” ?
8. Distinguish a General from a Qualified Acceptance.
9. Give three examples of Qualified Acceptances.
10. What is a “ referee in case of need ” ?
11. On 1st January, 19.., Messrs. Middlemiss & Turnbull, of London, sent to S. Macgregor, of Manchester, for acceptance, a Bill of Exchange for £100, dated 3rd January, 19.., and payable three months after date. S. Macgregor duly accepted the draft and made it payable at his bankers, The Staple and Stedfast Banking Co., Ltd., of Stockport.  
Show the form of the Bill as it would appear when returned to Messrs. Middlemiss & Turnbull ; and state who is the Drawer, and who is the Drawee ; and give the date when the Bill will mature.
12. What is an endorsement ?
13. Mention two kinds of endorsements.
14. Where is the proper place for the presentment of a Bill of Exchange ?
15. Explain the meaning of a dishonoured Bill of Exchange.
16. Distinguish between noting and protesting a Bill.



## CHAPTER XLIX

### CHEQUES

**A CHEQUE** is a bill of exchange drawn on a banker payable on demand. A cheque, being a bill of exchange, must necessarily be an unconditional order to pay a sum certain in money addressed by one person to another, viz. by the customer to his banker. A copy of a cheque, together with the analysis of its definition, is shown on page 586.

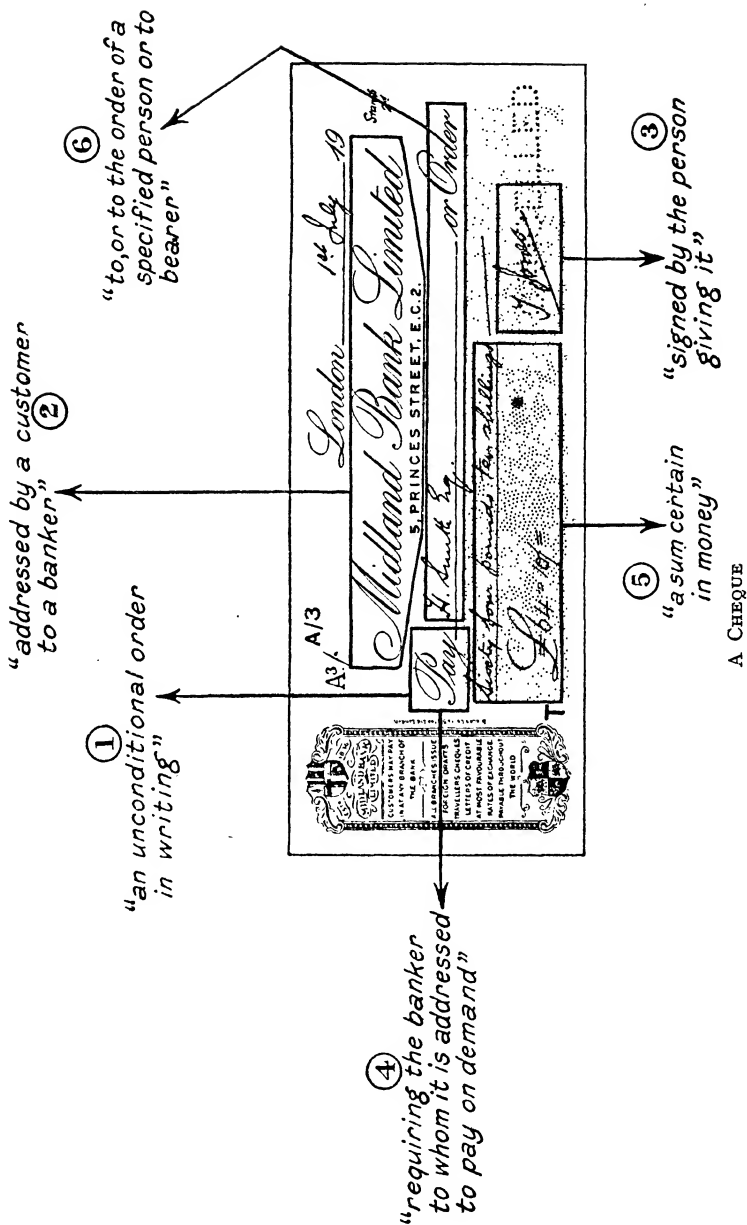
An instrument in the form of a cheque, but made payable only upon signature by the payee on the form of receipt at the foot of the instrument, is not strictly a cheque, because it is a conditional order.

A draft addressed by one bank to another branch of the same bank is not a cheque, since it is not addressed by one person to another.

For the most part, the rules applicable to those bills of exchange which are payable on demand apply also to cheques. No days of grace are allowed for the payment of a cheque, because it is always payable on demand.

**Cheques with Endorsed Receipts.** Of late years, many companies and other corporations have adopted an order for payment upon their bankers, requiring the payee to sign a receipt which is printed on the back of the cheque. By signing the receipt, the payee acknowledges that the debt of the company or corporation to him is discharged, and he could not afterwards bring an action for the amount. But if he simply endorsed a cheque on receiving payment, that would only prove that he had received a sum of money without showing for what purpose it had been paid. For some time, it used to be doubted whether such orders for payment were strictly cheques, since a condition was imposed of signing a receipt before the money would be paid by the bank. Recent cases, however, seem to show that the condition is not strictly imposed on the banker "not to pay," and, therefore, the order to the banker is unconditional. It has hitherto been a general practice among bankers to require from their customers who adopt cheques of this form an indemnity against any loss they may sustain in dealing with such cheques. The request for the indemnity has proceeded upon the assumption







that such orders for payment are not cheques in the truest sense of the word.

**Bearer Cheques.** A cheque is payable to bearer—

(1) When it is drawn payable to a specified person or to bearer, or even when no name is inserted, as : “ Pay ----- or bearer.” Whether the drawer inserts the name of a person or not, it is payable to bearer.

(2) When the only or the last endorsement is in blank.

(3) When the payee is a fictitious or non-existent person, i.e. when the name has no reference to any particular individual, such as : “ Pay Wages.” (Some authorities, however, consider such a cheque as payable to the order of the drawer.)

When a cheque is on the face of it payable to bearer, that is, when the word “ bearer ” appears on the front of the cheque, it cannot, by subsequent endorsement, be converted into an order cheque. For that reason, the endorsements of bearer cheques are not examined by the bank when such cheques are paid to the credit of an account. The word “ Order ” printed or lithographed on the cheque forms may be altered into “ Bearer ” by the drawer, but the alteration must be signed by him.

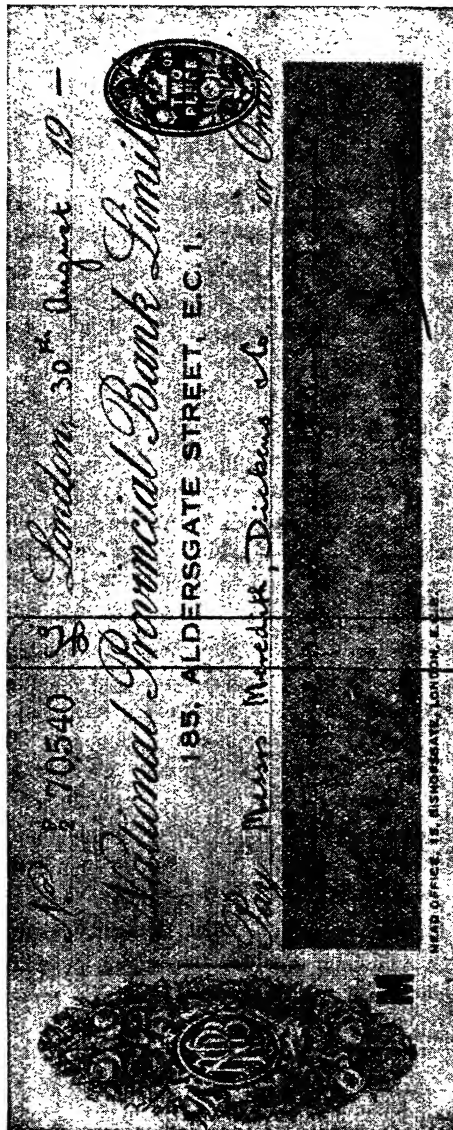
**Order Cheques.** A cheque payable to Charles Mitchell without the addition of the words “ or Order ” may be payable to Charles Mitchell personally without his endorsement. He may, however, endorse, and the effect of the endorsement is then the same as if the words “ or Order ” had been inserted. If the words “ Pay Charles Mitchell only ” or “ Not Transferable ” are put on a cheque, it cannot be paid to anyone else than the payee. These are called *restrictive* endorsements. When the payee of an order cheque writes his name on the back of a cheque, it is then endorsed in blank, and can be passed from one person to another without further endorsement. A blank endorsement may be converted into a special endorsement by writing over the endorser's signature the direction to pay some other person or Order, e.g.—

*Pay      David Woodhall      or Order.*

CHARLES MITCHELL.

Charles Mitchell writes his name on the back and passes it to David Woodhall ; but, before doing so, he writes : “ Pay David





A CROSSED CHEQUE



## EXAMPLES OF ENDORSEMENTS

- |  |  |
|--|--|
| <p>(1) <i>Joseph Shuttleworth.</i></p>   | <p>(1) Blank Endorsement.<br/>A cheque thus endorsed would be payable to "bearer."</p> |
| <p>(2) <i>Pay to the order of<br/>Mr. Leo Garner.<br/>Joseph Shuttleworth.</i></p>                         | <p>(2) Special Endorsement.</p>  |
| <p>(3) <i>Pay to Mr. Leo Garner<br/>only.<br/>Joseph Shuttleworth.</i></p>                                 | <p>(3) Restrictive Endorsement.</p>  |
| <p>(4) <i>Per pro. John Hall<br/>&amp; Son.<br/>Arthur Barr (Cashier).</i></p>                             | <p>(4) <i>Per procuration</i> Endorsement.</p>   |
| <p>(5) <i>James Kay,<br/>sole executor of the<br/>late Simon Caton.</i></p>                                | <p>(5) Executor's Endorsement,<br/>where there is only one executor.</p>               |
| <p>(6) <i>For Self and Co-<br/>Executors of Simon<br/>Caton.<br/>James Kay.</i></p>                        | <p>(6) The signature of one executor suffices to bind the rest.</p>                    |
| <p>(7) <i>For Leonard Garner.<br/>John Taylor } Trustees.<br/>Wm. Hall }</i></p>                           | <p>(7) Trustee's Endorsement.<br/>In this case, all the trustees would sign.</p>       |
| <p>(8) <i>HER<br/>Rose X Martin.<br/>MARK<br/>Witness, John Kay,<br/>40 Walkden Road,<br/>Worsley.</i></p> | <p>(8) Illiterate's Endorsement.</p>   |



Woodhall or Order." This will then become a *special* endorsement, because the cheque cannot be passed to anyone else unless David Woodhall's endorsement is there.

Although a cheque is payable to a named person who presents it, the banker takes the precaution of getting his endorsement. If the presenter is not the person named as the payee, and yet puts the payee's name as an endorsement on a cheque, he is guilty of forgery, and it is a forgery, although the name on the cheque is the same as that of the person named as the payee, provided, of course, that there are two different persons of the same name. The endorsement is evidence that the person who has endorsed it has received the cheque or has been paid the money.

The payee's cheque may be either *joint* or *alternative*. An example of the former would be: "Pay Charles Mitchell and Robert Mitchell." Both these persons must then endorse and both receive the money.

But in cases of partnership, one partner may sign for himself and the others. An alternative payee would be: "Pay Charles Mitchell or Robert Mitchell"; and in this case, either may endorse and either may receive the money.

Again, the cheque may be made payable to "A. B., or E. F. or Order," and the same rule will also apply in this case.

Another more obscure endorsement, which is not strictly joint or alternative, is as follows: "Pay the Trustees of John James or Order." This cheque must be endorsed by all the trustees, because trustees have no power to delegate their authority to one or more of their number, and each one must give his signature. One executor, however, may endorse for himself and co-executors.

**NEGOTIABILITY OF CHEQUES.**—A cheque can be negotiated like a bill of exchange, viz., by mere delivery, if payable to bearer; or by delivery, plus endorsement, if payable to order.

On the other hand—

(1) Cheques are never accepted by the drawee as in the case of bills of exchange. Hence, the holder of a cheque cannot sue the banker on whom it is drawn.

(2) Notice of dishonour to the drawer of a cheque is rarely necessary, because it is excused by the absence of any money belonging to the drawer in the hands of the drawee, which is the usual cause of the dishonour of a cheque.



(3) Cheques are not intended for circulation, as is the case with bills of exchange. Hence, a cheque must be presented for payment within a reasonable time of its issue; and in determining what is a reasonable time, regard must be had to—

- (a) the nature of the instrument;
- (b) the usage of trade and of bankers;
- (c) the facts of the particular case.

**PRESENTMENT FOR PAYMENT.**—In ordinary cases, if the receiver of a cheque and the banker on whom it is drawn are in the same town, it ought to be presented during the next day; and if they are in different towns, it ought to be forwarded for presentment during the next day and presented by the person to whom it is so forwarded within the day after he receives it.

Where a cheque is not presented for payment within a reasonable time of its issue and the drawer had the right at the time of such presentment as between himself and the banker to have the cheque paid, and suffers actual damage through the delay, he is discharged to the extent of such damage, that is to say to the extent to which such drawer is a creditor of such banker to a larger amount than he would have been had such cheque been paid.

E.g.—

A's balance on 1st May is £1,000.

A draws a cheque on 1st May for £800.

Cheque not presented for payment till 1st June.

On 20th May bank suspends payment.

A is a creditor for £1,000.

If cheque had been presented at proper time, he would have been a creditor for only £200.

Therefore, payee of cheque suffers the damage of the drawer.

On the other hand, the holder of a cheque as to which such drawer is discharged will be a creditor in lieu of the drawer of such banker to the extent of such discharge and will be entitled to recover the amount from the banker.

So long as the balance of an account is in the favour of his customer, a banker is bound, at his peril, to pay all cheques drawn by his customer; and if he fails in his duty, an action will lie against him, even though the customer has sustained no actual loss or damage in consequence of the dishonour of his cheque.

The only case where a banker having funds in hand is justified in refusing to cash a cheque is where by so doing he would be making himself a party to and therefore implicated in a breach of trust, viz., where he has notice at the time he cashes the cheque both—

- (1) That the fund on which the cheque is drawn is trust money, and
- (2) That his customer is attempting to deal with the fund in a manner inconsistent with the terms of the trust. In particular the fact of a personal benefit accruing to the banker as a result of the transaction would be strong evidence that the banker was privy to the breach of trust.



Payment by cheque is equivalent to payment in cash, subject to the condition that, if a cheque is stopped or dishonoured, the right of the creditor to receive payment in cash is revived.

If a cheque is sent by post in a letter properly addressed to a creditor and is lost in transmission, the debtor is discharged if he was directed by the creditor so to transmit the money, but not otherwise; and the mere fact that the debtor was following the usual course of dealing between the parties is not of itself sufficient to discharge him.

**COUNTERMAND OF PAYMENT.**—The duty and authority of a banker to pay a cheque drawn on him by his customer are determined by—

(1) Countermand of payment, which is usually called stopping a cheque. But in order that a countermand may be effective, there must be not only a change of purpose on the part of the customer, but also a notification of that change to the banker; and, although a telegram countermanding a cheque may reasonably be acted upon by a banker at least to the extent of postponing the honouring of a cheque until further inquiry can be made, yet a banker is not bound to accept an unauthenticated telegram as sufficient authority for the serious step of refusing payment.

(2) Notice of customer's death.

(3) Notice that the customer has committed an available act of bankruptcy.

(4) The receipt of a garnishee order.

**FORGED SIGNATURES OF DRAWER.**—Where a signature on a bill, cheque, or note is forged or placed thereon without the authority of the person whose signature it purports to be, the forged or unauthorised signature is wholly inoperative and no right either—

(a) To retain the bill, cheque, or note; or

(b) To give a good discharge therefor; or

(c) To enforce payment thereof against any party thereto can be acquired through or under that signature, unless the party against whom it is sought to retain or enforce payment of the bill, cheque, or note is precluded from setting up the forgery or want of authority. Hence—

(1) A banker who pays a cheque to which the drawer's signature has been forged cannot debit it to his customer's account.



(2) A banker who pays a cheque, the amount of which has been fraudulently altered or erased, can charge his customer only with the amount originally placed thereon, unless the customer has been so negligent in the discharge of some duty he owes to the banker as to be estopped from setting up the forgery as a defence. The extent of such duty depends upon the contract between the parties, whether expressed or implied from an established course of dealing between them ; but in 1918, the House of Lords held that if a customer of a bank draws a cheque in a manner which facilitates fraud, he is guilty of a breach of duty as between himself and the banker, and is responsible for any loss suffered by the banker as a consequence.

If a person signs his name on a blank stamped piece of paper and entrusts the paper to another person with authority to fill it up as a bill, cheque, or note for a certain amount, and that person fraudulently fills it up for a larger amount, the person first named will be estopped as against a bona fide holder for value of the instrument from denying the validity of the instrument, and will be liable for the full amount appearing on the face of the instrument.

**FORGED ENDORSEMENTS.**—The liability of a banker in the case of his paying a cheque bearing a forged endorsement was formerly the same as when he paid a cheque to which the drawer's signature was forged. But this was a hardship upon the bankers, because, while they may be expected to know their customers' signatures as drawers, they cannot possibly know the signature of every payee or endorsee, who may be entire strangers to them.

By the Bills of Exchange Act, 1882 (Sect. 60), when a bill payable to order on demand is drawn on a banker, and the banker on whom it is drawn pays the bill—

(1) In good faith ; and (2) In the ordinary course of business ; it is not incumbent on the banker to show that the endorsement of the payee, or any subsequent endorsement, was made by or under the authority of the person whose endorsement it purports to be ; and the banker is deemed to have paid the cheque in due course, although such endorsement has been forged or made without authority. But the provisions of this section of the Bills of Exchange Act have no application to—

(1) Forgeries of the drawer's signature.



(2) Any kind of instrument except a bill payable on demand, drawn upon himself, which is a cheque.

Hence a banker who pays any other kind of bill on the strength of a forged endorsement is still *prima facie* liable for any loss resulting therefrom.

(3) Any person other than the one on whom the cheque is drawn. Hence a third party who cashes a cheque bearing a forged endorsement, whether a banker or a private individual, is still *prima facie* liable to refund to the drawer the money received on the cheque from the banker on whom it is drawn.

**CROSSED CHEQUES.**—A cheque may be crossed either—

- (1) Generally;                      or                      (2) Specially.

A cheque is crossed generally when it bears across its face an addition of either—

(a) The words “and Company,” or any abbreviation thereof, between two parallel transverse lines; or

(b) Two parallel transverse lines simply.

A cheque is crossed specially when it bears across its face an addition of the name of a banker, in which case it is said to be crossed specially to the particular banker whose name appears on its face.

Examples of the different kinds of crossings are shown on page 595.

A crossing may be added to an uncrossed cheque by either the drawer or any holder of the cheque, either of whom may turn a general into a special crossing.

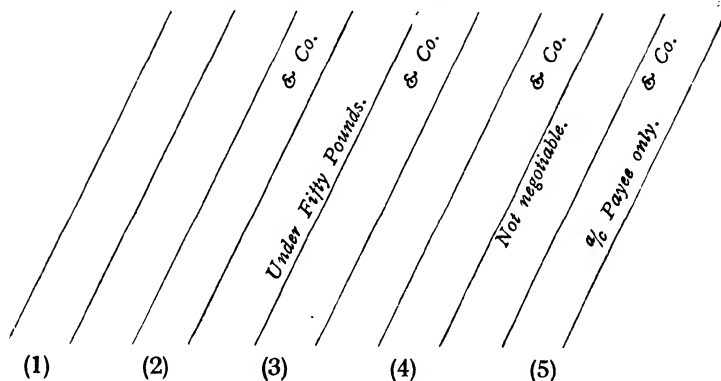
**Not Negotiable Crossing.** If and when a cheque is crossed, whether the crossing is a general or a special one, but not otherwise, it may also have the words “Not Negotiable” written across the face of it either by—

(1) The drawer; or

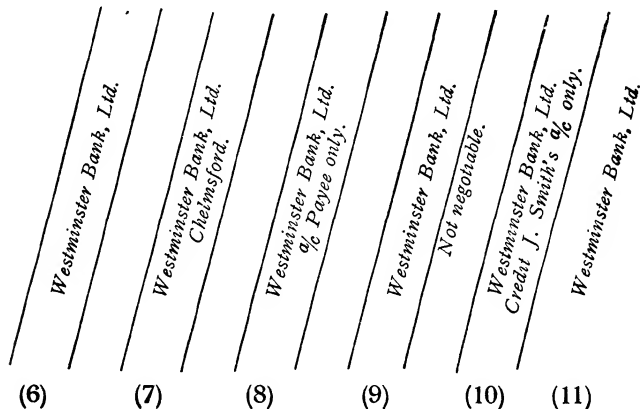
(2) Any holder of the cheque.

The effect of having the words “Not Negotiable” upon a cheque is that, although the cheque continues to be as freely transferable or assignable from one person to another as if those words had not been added, it ceases to be negotiable at all; and, therefore, a person who takes a crossed cheque which bears across its face the words “Not Negotiable,” cannot have, and he is not capable of giving, any better title to the cheque than the person from whom he took it had.



(a) *General Crossings*(b). *Special Crossings*

These are as under—

**RIGHTS AND DUTIES OF THE PAYING BANKER.**—Where either—

(1) An uncrossed cheque ; or

(2) A cheque crossed generally is sent to a bank for collection, the paying banker may cross it specially to himself ; and where a cheque is crossed specially, the banker to whom it is crossed may again cross it specially to another banker for collection.\* The general effect of crossing a cheque is to prevent its being paid except through the medium of a banker, because by the Bills of



Exchange Act, 1882 (Sect. 79), where a banker on whom a crossed cheque is drawn, pays it—

(a) If crossed generally otherwise than to a banker ; or

(b) If crossed specially, otherwise than to the particular banker to whom it is crossed, or to his agent for collection, being a banker ;

he is liable to the true owner of the cheque for any loss he may sustain in consequence of the cheque having been so paid.

On the other hand, where the banker on whom a crossed cheque is drawn, in good faith and without negligence, pays it—

(1) If crossed generally, to a banker ; or

(2) If crossed specially, to the particular banker to whom it is crossed, or to his agent for collection being a banker ; then both—

(a) The banker paying the cheque ; and

(b) The drawer of the cheque, *IF the cheque has actually come into the hands of the payee ;*

are respectively entitled to the same rights and to be placed in the same position as if payment of the cheque had been made to the true owner.

**RIGHTS AND DUTIES OF COLLECTING BANKER.**—Inasmuch as payment of a crossed cheque can be obtained only through the medium of a banker, it is only fair that a banker who collects a crossed cheque for a customer pursuant to a duty imposed upon him by law, should have a corresponding protection given to him by law while acting in the discharge of that duty.

Hence, by the Bills of Exchange Act, 1882 (Sect. 82), where a banker in good faith and without negligence receives payment for a customer of a cheque which is crossed either generally or specially to himself, and the customer has no title or only a defective title thereto, the banker will not incur any liability to the true owner of the cheque by reason only of having received such payment. Section 82, however, applies only to cheques which are crossed before they come into the banker's possession ; and the banker cannot, by afterwards crossing the cheque himself, become entitled to the protection given by the section.

In order that a collecting banker may be entitled to the benefit of Section 82, it is essential—

(1) That he should act in good faith and without negligence.



(2) That the person for whom he collects the cheque should be his customer, that is to say, a person between whom and himself there is some sort of account—though it is immaterial whether it is a current account or deposit account—or, at any rate, some similar relation.

The banker should act as a mere agent for the purpose of collecting the cheque for his customer. It was decided by the House of Lords, in 1903, in the case of *The London, City, and Midland Bank v. Gordon*, that if a banker credited a customer with the amounts of cheques as soon as they were paid into his account and allowed him to draw against the amounts so credited before the cheques were cleared, he did not act as a mere agent to collect the proceeds of the cheques for his customer, but he became a holder of the cheques on his own account and collected the proceeds for himself, so that he was not protected by Section 82 of the Act. But by the Bills of Exchange Crossed Cheques Act, 1906, a banker is now deemed to receive payment of a crossed cheque for his customer within the meaning of Section 82 of the principal Act, notwithstanding that he credits his customer's account with the amount of the cheque before receiving payment thereof.

**PROMISSORY NOTES.**—A *Promissory Note* is an unconditional promise in writing made by one person to another, signed by the maker, engaging to pay either—

(1) On demand; or

(2) At a fixed or determinable future time, a sum certain in money either to or to the order of a specified person, or to bearer.

A note which is, or on the face of it purports to be, both drawn and payable within the British Islands, is an inland note.

### PROMISSORY NOTE

<p><i>Stamp</i> 6</p> <p><u>£50-0-0</u></p>	<p>63 Wormwood Street London, E.C. August 15/19</p>
<p>Four months after date I promise to pay to Mr Harold Jeffery the sum of Fifty Pounds for value received.</p>	
<p>Ernest Roberts.</p>	



Any other note is a foreign note. Except as hereinafter mentioned, the provisions of the Bills of Exchange Act, 1882, relating to Bills of Exchange, apply with the necessary modifications to notes ; e.g.—

- (1) They are fully negotiable instruments ;
- (2) They can be negotiated by delivery with or without endorsement, as the case may be ;
- (3) The same days of grace are allowed ; and
- (4) Just as in the case of inland bills, so the paper on which inland notes are written must be previously stamped.

**DIFFERENCE BETWEEN PROMISSORY NOTES AND BILLS OF EXCHANGE.**—There are three points in which notes differ from bills, viz.—

(1) The stamp duty is *ad valorem* whether the note is payable on demand or otherwise.

(2) Whereas a bill has three original parties, viz., the drawer, drawee, and payee, a note has only two original parties, viz., the maker and payee.

(3) Whereas a drawer of a bill is only secondarily liable by way of surety to the acceptor, the drawer, or maker of a note is the person primarily liable, because the maker of a note, by making it, engages that he himself will pay it according to its tenor.

Hence, in applying the provisions of the Bills of Exchange Act to Promissory Notes, two points must be borne in mind—

(1) The maker of a note is deemed to correspond not with the drawer, but with the *acceptor* of a bill.

(2) The first endorser of a note is deemed to correspond with the drawer of an accepted bill payable to the drawer's order.

On the other hand, the following provisions of the Act relating to bills do *not* apply to notes—

(1) Provisions as to acceptance, including presentment for acceptance and acceptance *supra protest*, because a promissory note is never accepted.

(2) Provisions as to bills in a set, because the practice of drawing notes in a set is unknown.

(3) The protesting of foreign bills, because when a foreign note is dishonoured, the protest thereof is unnecessary.

**Joint and Several Promissory Notes.** A promissory note may be made by two or more makers, and they may be liable thereon either—



(1) Jointly ; or (2) Jointly and severally.

But where a note runs : " I promise to pay," and is signed by two or more persons, it is deemed to be their joint and several note.

Presentment for payment is always necessary to render an endorser of a note liable ; but it is not necessary to charge the maker of a note, except where the note is made payable at a particular place.

### JOINT AND SEVERAL PROMISSORY NOTE

Stamp if.  <u>£85.0.0</u>	25 Gracechurch Street, London E.C. August 15 <sup>th</sup> 19
<p><i>Three months after date we jointly and severally promise to pay to John Roberson or order the sum of Eighty Five pounds for value received.</i></p> <p><i>Ernest Roberts.</i>  <i>James Brown</i></p>	

"I OWE YOU."—An instrument which is sometimes confused with a promissory note is an I O U , but the essential difference between the two is that a note is a negotiable instrument, whereas an I O U is not ; that is to say, the rights arising under an I O U can only be assigned from one person to another under and subject to the conditions of the Judicature Act, 1873.

An I O U is a mere acknowledgment in writing of a debt due from the person who gives it, to the person to whom it is given. But although it is evidence of some debt being due, it is not evidence of the nature of the debt (e.g. whether it was for money lent or for goods supplied, or for services rendered or otherwise).

An I O U in the ordinary form does not require any stamp ; but—

(1) If it contains an agreement that it is to be paid on a fixed day or on demand, it will amount to a promissory note, and must be stamped as such ; and

(2) If the words used are such as to make it not a promissory note, but an ordinary contract to pay money, it must be stamped with a sixpenny agreement stamp, unless it is under £5 in amount.



## TEST PAPER XLIX

1. Is a draft by a Bank to its Branch, a cheque? Give reasons for your answer.

2. What is the effect of "crossing" a cheque, and what is the difference between a cheque made payable to Tom Jones or "order" and one payable to Tom Jones or "bearer"?

3. What is a restrictive endorsement?

4. How may a blank endorsement of a cheque be converted into a special endorsement?

5. Draw a cheque on the Westminster Bank, Ltd., in settlement of an account. Cross it generally and mark it "Not negotiable." Explain the effect of the last two words.

6. How does the negotiability of a cheque differ from that of a Bill of Exchange?

7. When should a cheque be presented for payment?

8. What authority has a banker to stop payment of a cheque?

9. Explain the following terms—

Bearer

Special Endorsee

Holder in due course

Acceptor *supra protest*

10. Explain and contrast the advantages or disadvantages of the understated crossings as used in connection with cheques—

*Not Negotiable*

*Alc Payee only*

11. What is meant by "crossing" a cheque, and why is it resorted to? Give three different specimen crossings, and explain the meaning of each. If you received an open cheque made out in your name and payable to bearer, what precautions would you adopt to prevent its being wrongfully cashed?

12. What is the effect of crossing a cheque "Not Negotiable"?

13. What are the rights and duties of the "paying banker"?

14. What is the effect of a forged or unauthorised signature on a cheque?

15. Explain the terms—

*General crossing.*

*Collecting banker.*

*Forged endorsement.*

16. What special rules apply to bankers in dealing with crossed cheques?

17. What is the difference between a Promissory Note and a Bill of Exchange?

18. What is a Joint and several Promissory Note?

19. A B owes C D £100, payment of which the latter agrees to allow to stand over for six months on receiving interest at £4 per cent. per annum. Draw up a promissory note to carry out this arrangement.

20. Messrs. J. Jones & Co., Ltd., Cardiff, owe to Messrs. T. Williams & Son, Newport, £350.

(a) Draw a cheque on Lloyds Bank, Ltd., dated 1st April, to discharge this debt. Cross the cheque specially.

(b) Draw a bill of exchange, dated 1st April, payable in three months after date to discharge the same debt. Show the acceptance of the bill.

Point out as many differences in the two forms of payment as you can.



## CHAPTER L

### THE BANKERS' CLEARING HOUSE

THE amount of money which changes hands daily in the City of London averages over 120 millions of pounds sterling in cheques and bills, exclusive of cash payments; and the value of the English banking facilities will be further understood when it is learned that this sum is passed from hand to hand without the handling of a single coin of the realm. This is made possible by the existence of the London Bankers' Clearing House, through which pass the majority of the cheques drawn on banks in England and Wales.

**THE CLEARING HOUSE SYSTEM.**—This system appears to have arisen in an unofficial manner, concurrently with the use of cheques and the growth of deposit banking in London. Every day clerks had to go round to each of the other banks to present cheques and bills upon them and bring back the proceeds. It soon became evident that much time could be saved if, instead of going to each bank separately, they were to meet in one central place and make their settlements together. The practice of doing so appears to have begun about 1770. The development of this system justified the building of a Clearing House in Post Office Court, Lombard Street, in 1833. Originally thirty-nine private banks combined in this arrangement, and it was not until 1854 that the joint stock banks obtained admission. By the end of the nineteenth century, however, the number of private banks had so diminished—due partially to the failure of some of the larger Houses in successive banking panics and crises—that the joint stock banks had become the owners of the Clearing House. These banks carried with them the development of the system of payment by cheque; until at the present time the volume of commercial transactions carried out purely by cheque is many times as great as that completed in notes and coin.

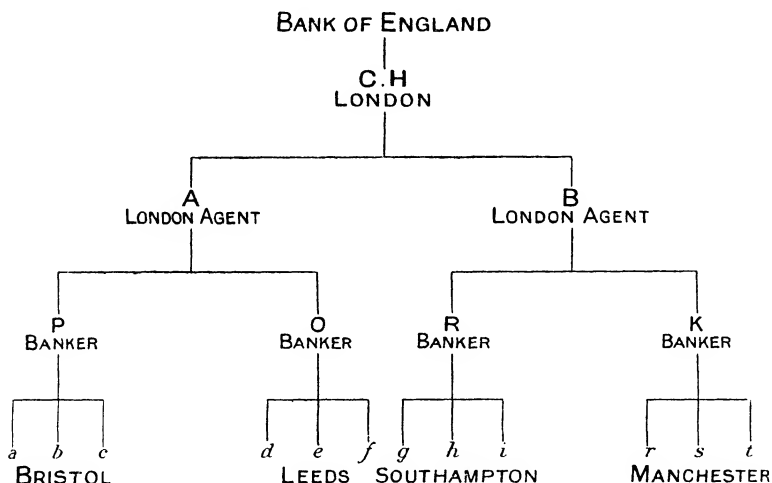
The Clearing House itself is regulated by rules which are drawn up by a committee of members, and administered impartially by the officers, viz. the chief inspector, the deputy inspector, and the assistant, all of whom are appointed by the committee.

Each clearing bank has an account with the Bank of England, where the "Account of the Clearing Bankers" is also kept. At



the close of each day's business, when the balance due to or from the Clearing House in respect of each individual bank has been ascertained, the amount is transferred to or from the "Account of the Clearing Bankers," and the account of the individual bank.

**PRINCIPLE OF CLEARING.**—In the diagram below, let A be the London agent of P and O; B the London agent of R and K, C. H. representing the London Clearing House. If *b*, a customer of P in Bristol, sends a cheque to S, a customer of K in Manchester, S would pay the cheque into K for collection; K would



then credit S with the amount, and forward the cheque to the London agent B, who would debit A and credit K, presenting the cheque on A through the Clearing House. A would then debit P and credit B, forwarding the cheque to P by the next post; P, on receiving the cheque, would debit his customer *b*, and credit the Agent A, the transaction again being closed.

Thus, since every London bank has a running account with the Bank of England, the balance to be paid from one bank to another on each day's clearing is settled by a cheque on the Bank of England, where a simple transfer in the books from one account to the other closes with simplicity and perfection all the daily payments made from one part of the kingdom to another.

**CLEARING BANKS.**—In 1854 payment of differences in money as



between bankers was abandoned and an account was opened by each member bank at the Bank of England. In 1858 country cheques (except certain local ones) came to be passed through the London agent of the country bankers. In 1864 the Bank of England joined the Clearing House.

In addition to cheques, bills of exchange and promissory notes in London (but not country bills or notes) are free to pass through the Clearing House. In addition to the "Big Five" the present members of the Clearing House are the Bank of England, the National Bank, Martins Bank, Coutts & Co., Glyn, Mills & Co., Williams Deacon & Co., and the District Bank. The Bankers' Clearing House Returns form a valuable indication of the conditions of trade. As our internal transactions in trade are completed by means of bills and cheques, the range of clearing, as it is termed, furnishes a direct indication of the volume of those transactions—that is, of the activity or depression of trade.

In addition to the London Clearing House there are provincial clearing houses at Birmingham, Bristol, Leeds, Leicester, Liverpool, Manchester, Newcastle, Nottingham, and Sheffield. Each one clears cheques within its own town and the area surrounding it.

The settlement of mutual dealings through the London Clearing House is dealt with by means of summarised sheets, i.e. printed lists with debit and credit columns showing the liabilities of the individual banks to the bank whose name appears at the head of its own list.

These summary sheets are compiled after the four clearings for each day have been effected. The four clearings are—

(1) **Metropolitan**—cheques drawn on the branches of Clearing Banks situated in London.

(2) **First Town Clearing**—cheques drawn on the Clearing Banks and received since the closing of the Clearing House of the previous day.

(3) **Country Clearing**.—cheques drawn on country banks.

(4) **Second Town Clearing** (the busiest of all)—cheques drawn on members of the Clearing House and paid in during the morning, and also cheques received from suburban and branch banks during the morning.

For convenience in sorting the instruments dealt with are distinguished by the letters "T," "M," or "C" which is printed in the left-hand corner of each cheque.

Each Clearing Bank has an account at the Bank of England, and



## SPECIMEN CLEARING TRANSACTION

Example—

£                      £  
 A owes to B 300, to D 400  
 B    "    C 100,    D 100  
 C    "    D 250,    A 100  
 D    "    B 60,    C 40

(In the Books of the Clearing House)

A		B		C		D	
Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
To B . £ 300	By C . £ 100	To C . £ 100	By A . £ 300	To D . £ 250	By C . £ 100	To B . £ 660	By A . £ 400
" D . 400	" Bal. 600	" D . 100	" D . 60	" A . 100	" D . 40	" C . 40	" B . 100
		" Bal. 180		" Bal. 210	" Bal. 210	" Bal. 650	" C . 250
£ 700	£ 700	£ 360	£ 360	£ 350	£ 350	£ 750	£ 750
To Bal. 600		By Bal. 180		To Bal. 210		By Bal. 650	

## CLEARING HOUSE SUMMARY

Debtors		Creditors	
Summary Sheet { A . £ 600	B . 160		£ 160
{ C . 210	D . 650		£ 650
			£ 810

(In the Books of the Bank of England)

## GENERAL CLEARING HOUSE ACCOUNT

Dr.		Cr.	
To B . £ 160	By A . £ 600		
" D . 650	" C . 210		
£ 810	£ 810		

## CLEARING BANKERS ACCOUNTS

A		B		C		D	
Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
To C.H. A/c . £ 600		By C.H. A/c . £ 160		To C.H. A/c . £ 210			By C.H. A/c . £ 650

The amount of £810 is not paid in cash but the accounts of B and D are credited in the books in the Bank of England, whilst those of A and C are debited. For these amounts special tickets are issued, white tickets for credits and green for debits. Both tickets are signed by an Inspector at the Clearing House to certify their correctness.

The above example is an attempt to illustrate the economy of time and effort resulting from the operations of the Clearing System. Instead of currency changing hands, debts are set-off against one another through the Bank of England.



there is also a general account known as the Clearing Bankers' Account. If, on any day, a bank is indebted to the others on balance, a white ticket is made out to effect a transfer from its account at the Bank of England to the Clearing Bankers' Account. If, on the other hand, it is in credit, a green ticket is used to authorise a transfer from the Clearing Bankers' Account to the bank's own account at the Bank of England. Both tickets are signed by an inspector at the Clearing House to certify their correctness. If there are any "returns," i.e. dishonoured cheques, they are sent back to the Clearing House before 4.10 p.m. on the day of exchange if they are London cheques. Country cheques, however, are returned by the paying bank direct to the banker on whom the cheque was drawn and a settlement in respect of such cheques is made without subsequent resort to the Clearing House, though the London agents have to be informed of the fact of dishonour. A specimen transaction is shown on page 604. The amount of transactions varies from 200 to 300 millions of pounds sterling each week, while in New York, until the slump of 1929, the volume of the cheque was roughly £1,000 millions per week. The extent of the bankers' clearings are an indication of the state of trade and of financial activities from year to year.

Clearing houses similar to those of the provinces exist in Scotland and Ireland, and in Scotland a considerable number of the notes issued by the Scottish banks are passed through in addition to cheques. Up to the present there is not one clearing house for all three countries, and this is a great drawback, incurring financial loss.

The New York Clearing House is worked on lines similar to London except that a large part of the balances between clearing banks is settled by means of clearing house gold certificates. These certificates are issued in exchange for coin deposited by the member banks in the vaults of the New York Clearing House, but the certificates can be used only for settling differences.

**OTHER CLEARING HOUSES.**—The clearing system has been found advantageous in several other circles apart from banking. For example—

(a) The Railway Clearing House, situated near Euston Station, employs a staff of about 2,000 persons, and is engaged in striking the balances between the various companies in respect of their bookings and similar dealings.



(b) The London Produce Clearing House regulates bargains in foreign and colonial produce, such as tea, coffee, wheat, and other products.

(c) The Cotton Clearing House at Liverpool deals specially with the trade in raw cotton.

(d) The Stock Exchange Clearing House eliminates all intermediary buyers and sellers of securities in the course of a fortnightly account, and ultimately reveals the original sellers of stock and the eventual buyers.

The profits or losses made by intermediate dealers are settled by means of "differences." All clearing methods are of service to the community because they vastly reduce the amount of circulating media required by the community.

### TEST PAPER I

1. Explain the reason why so much business is effected on such a small cash basis.

2. Into what four classes are the London Clearings divided?

3. Distinguish between Town, Country, Metropolitan, and Provincial Clearings.

4. Copy the diagram on page 602 and explain carefully its meaning.

5. Mr. Jones, who banks with Thompson & Co., buys goods from Mr. Brown, who banks with Williams & Co., and pays for them with a cheque. Explain the nature of that cheque; and trace its life-history from the time when it is signed by Mr. Jones to the time when it returns to him in his pass-book.

6. Show by simple illustrations, the economy of time and labour effected by the use of the bankers' clearing houses. If there take place a large increase in the trade of the country, and a steady fall in wholesale prices, how would you expect these factors to be shown in the figures of the bank clearing?

7. A B, who has a banking account with Barclays Bank, Threadneedle Street, London, hands a cheque for £100 to C D, who banks with Lloyds Bank, Cornhill, London. State as clearly and fully as possible what happens to this cheque, and through whose hands it passes. In what respect, if any, would your answer have been different if A B had his banking account with the Bank of England?

8. Give a simple illustration of the work of a bankers' clearing house. What deductions can be drawn from changes in the periodic figures of total clearings?



## CHAPTER LI

### THE FOREIGN EXCHANGES

FOREIGN Exchange may be defined as that section of commerce which deals with the means and methods by which rights to wealth expressed in the currency of one country are translated into rights to wealth in terms of another country's currency. It is simply an extension of the internal credit system to the wider field of international trade, and is rendered necessary by the existence of different national monetary systems. If we have a group of countries each member of which defines the value of its unit of account in terms of the same metal, say gold, then it would be possible for international indebtedness to be settled by the transmission of gold from debtor to creditor. This method, even in normal times, would be both inconvenient and expensive, and has, in modern times, accounted for only a very small fraction of international payments. The system of the foreign exchanges provides a means for the settlement of indebtedness between traders in different countries, not by the transfer of metallic money, but by the use of credit instruments. Debts and credits which are near together are made to settle debts and credits which are far apart. Indeed, foreign exchange has been described as the sale of bank deposits in one country in order to acquire control of bank deposits abroad.

The basis of this international indebtedness is foreign commerce, which may assume a number of different forms, the chief of which are—

- (1) Payments for the imports and exports of commodities, that is, raw materials and finished goods, which pass between one country and another.

- (2) Payments for services rendered, such as transport, banking, insurance, or the provision of tourist facilities.

- (3) The making of loans to foreign governments and other bodies, and the repayment of principal and interest.

- (4) Investment in industrial and commercial enterprises abroad and the payment of dividends.

- (5) Purchase and sale of stock exchange securities of international importance.



**THE MACHINERY OF SETTLEMENT.**—So far as the internal trade of a country is concerned, a debtor may pay his creditor either by the use of legal tender money or by the use of some credit instrument such as a cheque. When we come to the question of foreign trade, however, ordinary legal tender money cannot be used, so that we are compelled either to find some commodity which is acceptable, such as gold, or to deal in credit instruments through some international clearing system. The use of bullion for this purpose has practically been abandoned for reasons which the following example

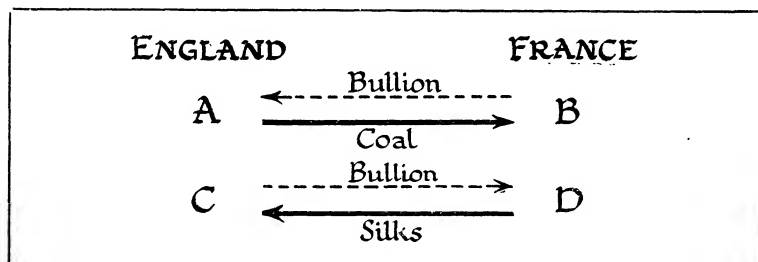


FIG. 1. PAYMENT WITH BULLION

will make plain. Suppose, as in Fig. 1, that A in England, is creditor to B in France for a certain sum; suppose that D in France is creditor to C in England for an equal sum; then, in order to pay their debts by this method, B would have to send bullion to A, and C would have to send an equal sum to D, thus causing two separate transmissions of bullion between England and France at considerable expense to both parties.

Let us now imagine that a bill of exchange is introduced into the transaction as in Fig. 2. B gives his acceptance to A for the amount of the debt, and the latter sells the bill to C. A has now received his money and drops out of the transaction. C, in turn, sends the bill to D in France in settlement of his debt, and D presents it to B for payment. Thus, under this arrangement, C pays A in England, and B pays D in France, with a saving of trouble and expense to all parties. We may imagine a bank or a bill broker acting as an intermediary in both countries in order to establish contact between the parties.

Even in the latter example, however, we have made an assumption which is highly improbable, namely, that the debt between A and



B is exactly equal to that between C and D, so that the bill can be transferred from A to C. In order to overcome this difficulty, let us carry the argument a stage further. Suppose that the English bank buys remittances from France from all those who wish to sell them and pays out sterling for them. The remittances are sent to France, either to a branch or a correspondent bank, and the proceeds, in francs, when collected, are credited to the English bank's account in France. If, now, other customers in England wish to pay debts in France, the English bank can sell to them, in exchange

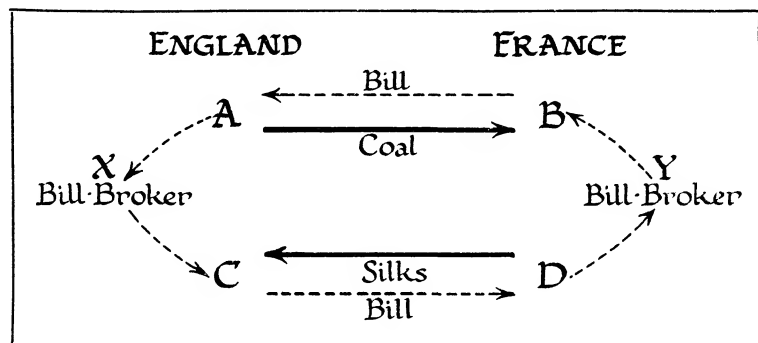


FIG. 2. PAYMENT WITH BILL OF EXCHANGE

for sterling, claims in francs drawn upon the account which has been built up in France. In like manner, the French correspondent bank will maintain a sterling account and will act in the same way, so that between them they provide a clearing house for the settlement of Anglo-French debts.

**BILLS DRAWN ON LONDON.**—Bills of Exchange may be accepted and made payable at any place whatsoever, but the custom has grown up in England which requires them to be made payable in London. This is partly necessitated by the banking system, for the vital requisite of the securities in which the banks invest this portion of their deposit money is *negotiability*. The securities must be readily convertible into money in case of need; and to render bills thus convertible, they must be payable in London—the discount centre of England.

The universality of English exports also causes bills drawn on London to be in great demand. In all parts of the world,



there are always merchants who have imported goods from England and who are only too pleased to get an English bill drawn on London to pay for them. Another reason why bills on London are in great demand abroad is the fact that the English bill is always negotiable in gold of the  $\frac{11}{12}$ ths caratage, that is to say, of the finest caratage in the world. It is, therefore, for this reason that England accepts much and draws but little.

It is the English bill with the English acceptance upon it that does the bulk of the work of the commercial world. The acceptance of an English banker is regarded all over the world as a guarantee that the bill will be met at maturity. Another factor in favour of a bill on England is the universality of the exports of England. It is not merely the magnitude, but the universality of our exports which renders English bills so important, for in every port there is always some merchant willing to purchase a bill on London, because he wants to pay for English goods.

The rate of exchange is, therefore, fixed abroad, and England has little influence in determining what it shall be. The bill is drawn abroad and is sold for what can be obtained for it abroad, so that the bill finds its origin and its value in the foreign port.

**MINT PAR OF EXCHANGE.**—When the price of a bill is at such a rate that an ounce of fine gold in one country commands the right to receive one ounce of fine gold in another country, the exchange is said to be at Mint par. This does not by any means imply that the exchange enables an ounce of foreign coin to exchange for an ounce of English coin, because the caratage of the two coinages may be different. The caratage means the proportion of fine gold in the currency. English caratage is 22, which means that 22 out of 24 (or  $\frac{11}{12}$ ) are fine gold. In the English sovereign,  $\frac{11}{12}$ ths of the weight are pure gold. In the French 20 franc piece,  $\frac{9}{10}$ ths are pure gold. In the German Reichmark  $\frac{9}{10}$ ths are pure gold. There is practically only one other country of the  $\frac{11}{12}$ th standard, and that is Turkey.

When the exchange is at Mint par, it is at such a point that an ounce of fine gold commands an ounce of fine gold in another country, "fine gold" being the technical word for pure gold. When the exchange is at Mint par, it is held to imply an equality between the supply of and demand for bills.

The amount of fine gold in the currency of a nation is fixed by



the currency laws of that nation. According to the Currency Act of Lord Liverpool in 1816, the proportion of fine gold in the English currency is 11 out of 12, but that is not the case with regard to other countries. The law of those countries must be known in order to find the Mint par, which then must be calculated by that process of Arithmetic known as the Chain Rule.

*Example :* Find the Mint par between England and Switzerland.

How many francs	= 1 sovereign (?)
1 sovereign	= 7.98805 grammes
If grammes, English standard	} 12 = 11 grammes fine
If grammes fine	
900	= 3,100 frs.

$$\text{The result is } \frac{7.98805 \times 11 \times 3100}{12 \times 900} = 25.2215 \text{ frs.}$$

Again, what is the value of the sovereign expressed in marks, if 500 grammes of pure gold are converted into  $69\frac{3}{4}$  twenty-mark pieces  *$\frac{9}{10}$ th fine*?

How many reichmarks	= 1 sovereign (?)
If sovereign	1 = 7.98805 grammes standard
If grammes standard	12 = 11 grammes fine
If grammes fine	500 = 1,395 reichsmarks

$$\therefore \frac{7.98805 \times 11 \times 1395}{12 \times 500} = 20.43 \text{ marks}$$

When two countries have different metals in their currencies, as, for instance, when one country is a gold-using country (e.g. England) and another is a silver-using country like China, there is no Mint par ready made, but it can always be calculated for any given day by using for that day the gold price of silver or the silver price of gold, as the case may be.

Between countries of different currencies there is a calculable par, so that it is incorrect to say there is no par. The same remarks hold with regard to paper. For example, there may be a 20 per cent. depreciation of paper in Venezuela; that is, for £100 bill: what is the par price in London? If the bill were taken by a merchant in Venezuela, it would be sold in the open market of Venezuela for bullion to the extent of £80. The par



of exchange as between London and Venezuela is £80 for £100 bill. Eighty sovereigns in London will purchase paper of the nominal value of £100.

**GOLD POINTS.**—The gold or specie points may be defined as those rates of exchange at which settlement of international debts may be made as cheaply by the use of gold as by using credit instruments. Hence it follows that under an effective gold standard system, these points represent the limits of exchange fluctuation between gold currencies. The aim of a debtor who has to make a foreign payment will be to use the cheapest method at his disposal, and consequently he will usually employ some form of credit instrument. If he were to effect a settlement in gold, he would have to pay the cost of brokerage, packing, freight, and insurance, added to which he would lose interest on the sum involved during the time the gold was in transit. If, however, the demand for remittances in a particular currency is great, the rate for buying them may rise to such an extent that it is cheaper to bear these costs and pay in gold. If this course is practicable, it will be adopted. The *gold export point* is therefore the exchange rate at which gold will tend to leave a country, whilst the *gold import point* is the rate at which it will tend to come in.

Since the widespread abandonment of the gold standard, the specie points are mainly of academic significance, though they are operative between such countries which are still on the gold standard. Even when gold movements are possible, however, it should not be imagined that it is ordinary merchants themselves who take the initiative in shipping gold. Such transfers require highly specialised knowledge and experience, and are therefore undertaken by banks and bullion brokers. The following are the main factors which require consideration when arranging a gold shipment between two centres—

(1) The price at which gold can be bought and sold in the two centres is of prime importance, since upon these prices the gross profit of the shipment depends.

(2) Different countries have varying standards of fineness for their standard gold, so that when bullion is transferred from one country to another, expenses in connection with refining may be incurred. Assaying charges may also be made by the buying authority.

(3) The cost of transporting the gold between the two centres



must be allowed for. Usually a "through" rate will be quoted, based on the declared value of the consignment.

(4) The gold must be insured against risk of loss whilst in transit.

(5) When gold is purchased for shipment, cash must be paid immediately, but no foreign currency is received until the shipment arrives in the foreign centre. Allowance must therefore be made for the interest lost on the funds locked up in the consignment until payment is received.

(6) Miscellaneous expenses may be incurred, such as brokerage when the bullion is bought through a dealer in the London market, or packing and boxing charges.

The gold points, when operative, must not be regarded as having a rigidly fixed relation to mint parities. Freight rates are more favourable when large quantities are shipped, whilst insurance rates tend to be higher when a large quantity is shipped on a particular boat. Since 1918, incidental expenses have proved to be a very uncertain item. Thus, in the past, the Federal Reserve Bank has delivered gold for approved shipments on a f.o.b. basis, but this concession was not granted where it was sought to discourage a particular shipment. Again, a central bank, and sometimes even a commercial bank, has disregarded the factor of interest in arranging a shipment. All these factors have contributed to the instability of the gold points since the War.

**METHODS OF REMITTING FUNDS.**—We have already defined the business of foreign exchange as being concerned with the settlement of foreign debts by the use of credit instruments. For this purpose, foreign exchange dealers have evolved a number of different types of remittance, which differ one from the other mainly in the speed with which they can be converted into cash, and the risks to which they expose the user. The following are the principal types—

(1) **Telegraphic or Cable Transfers.** These are orders for the payment of foreign currency which are sent by telegraph or cable. They may be used when it is desired to settle obligations in foreign money immediately, and thus avoid the delays incidental to sending remittances by mail. Sterling is paid into the bank when the order to make payment is given, and the foreign currency is paid over to the creditor on the same day. Such a method of payment obviously can be used only between institutions holding funds on deposit with one another. Further, an elaborate system of authenticating cables



must be devised in order to avoid the possibility of fraud, and this is possible only between banks with working agreements. The telegraphic transfer is the safest and most convenient mode for the transmission of funds, and therefore commands the best rate. Indeed, the T.T. rate is the basic rate of exchange between two currencies.

(2) **Mail Transfer.** This is an order sent by one bank to another, by mail, instructing it to pay over a sum in currency to a third party and debit the bank's currency account with the amount and the charges. In effect, this instrument operates in the same way as a cheque, but since it is not negotiable or transferable, there is no stamp duty, and there is no risk of loss. Payment of funds in the foreign centre will, however, be delayed until the arrival of the instrument, so that some allowance must be made in the rate for loss of interest.

(3) **Guaranteed Mail Transfer.** This is an instrument of comparatively recent origin designed to remove the element of uncertainty as to the time of payment associated with the use of a mail transfer. Payment of a mail transfer cannot be made prior to the arrival of the instrument itself, so that an unexpected delay in the mail will upset the basis of the allowance for loss of interest to the detriment of one or other of the parties. In order to make the date of payment of the funds in the foreign centre certain, the guaranteed mail transfer is employed, which is sold with an undertaking that the funds shall be paid over on a stated date, irrespective of the arrival of the mail. Instructions are sent to the bank overseas by "deferred" cable, that is, during slack hours, at cheaper rates.

(4) **Stock Draft.** This is a draft drawn by a seller of stock exchange securities in the home centre upon the buyer abroad. The relevant securities are attached to the draft so that the purchasing bank has a lien on them for the amount of the draft as well as preserving his right of recourse against the customer as drawer of the cheque. Suppose, for example, that a firm of London stockbrokers makes a purchase of shares on behalf of a client in New York. They draw on him for the amount of the purchase and sell the draft to a London bank with the stock certificates attached. The London bank collects the amount of the draft in dollars for the credit of its account in New York. If the reverse transaction takes place, the buyer in London may make arrangements with his bank to pay over to the



seller of shares in New York the amount of the transaction in dollars against delivery of a draft with certificates attached. Such a document is known as a *reverse stock draft*.

(5) **Bill of Exchange.** These may be classified as to type into bank bills and trade bills, and as to tenor into long bills and short bills. A *bank bill* is a bill of exchange carrying the name of one or more recognised London banks or accepting houses. A *trade bill* is one drawn in connection with the sale of goods. The description may be even more precise, so that a "cotton" bill is one drawn against a sale of cotton. A *long bill* is one drawn payable at more than thirty days after date or sight, whilst a *short bill* is one drawn at less than this period, or which has not more than this time to run before maturity. When a bill is originally drawn against a shipment of goods, it usually has attached to it the documents of title to the goods, such as the invoice, the bills of lading, the insurance policy, and certificate of origin, so that the holder of the bill possesses a lien over the goods until he is assured all is in order. Bills with these documents attached to them are called *documentary bills*, whereas once the documents have been detached, the bills are known as *clean bills*.

**RATES OF EXCHANGE.**—These are the rates published in the newspapers, and are the basis upon which remittances are made. The quotations mean that if a person wished immediate payment to be made he would hand over to a banker in London the required amount in sterling, and the banker would thereupon instruct his branch or correspondent abroad by telegram to pay the equivalent in currency at the rate indicated to a named person in that city as soon as the telegram had been received there and had been decoded. The rates at which these deals go through are called "cable rates" since the orders to the foreign agents for their execution are sent by cable. For large sums, say £2,000 and upwards, no charge is made for the cable. In other cases the remitter is expected to pay the cost of the wire. The table on page 617 has been taken from *The Times*. It will be noticed that each place has two quotations, which purport to be the highest and lowest of the day. Sometimes these two limits represent the buying and selling prices. The *Daily Telegraph*, on the other hand, gives the closing rates for buyers and sellers. Thus the practice varies with different newspapers. For purposes of explanation, however, we may take the



quotations as buying and selling prices for the respective foreign currencies. The first part of each quotation is the price offered by the buyers and the other rate is the sellers' price; the one may be taken to indicate the demand for and the other the supply of exchange. A little explanation will make this clear. The first rate, representing the lower quotation, means that the buyer will offer as low a price as possible, while the seller tries to obtain the higher price. For instance, if the holder of French francs wants to exchange them for sterling, theoretically he will strive to get the higher rate—he will want as many pounds, shillings and pence as he can get for the fewest francs—so he will offer 124·22. Likewise the person who has sterling to sell will endeavour to get as many francs as he can—he will bargain on the basis of 124·26. But, as already mentioned, the reverse position will hold good with the pence rates. The person who is buying exchange on Monte Video will endeavour to get his wants supplied at  $43\frac{1}{4}$  pence; he will surrender less pence per foreign unit; but the seller of the foreign currency will endeavour to get  $43\frac{3}{4}$  pence. The person operating in the foreign country will obviously need to work the other way round. If he is a buyer of sterling in Paris he will try to surrender as few francs per pound as he can, while if he is a seller of sterling he will try to get as many francs for each pound. Likewise with the pence rates. In the case of Calcutta, for example, 1s.  $5\frac{2}{3}\frac{1}{2}$ d. per rupee will be a worse rate for a buyer of sterling than 1s.  $5\frac{3}{4}$ d. since he will have to give more rupees for our currency, or in other words receive less sterling.

**RELATIONS BETWEEN EXCHANGE RATES.**—The foregoing figures are based on the cable rate, that is the rate for the purchase and sale of *telegraphic transfers* which forms the foundation of all exchange dealing. This rate is not, however, applicable to the other forms of credit instrument which we have enumerated above, and special rates have to be calculated in respect of them. In the first place, we have what is termed the “cheque” or “demand” rate, which may be defined as the rate applied to the purchase or sale of a bill payable at sight, such as a guaranteed mail transfer. As we have seen, in the case of such an instrument, allowance must be made for loss of interest. When a London bank buys such an instrument from a customer it pays out sterling immediately, but does not obtain the use of the foreign currency until a certain time has



## LONDON RATES OF EXCHANGE

Place	Method of Quoting	Par of Exchange	Feb. 24	Feb. 22
New York . . .	\$ to £	4.86 $\frac{3}{4}$	4.86 $\frac{1}{8}$ —4.86 $\frac{5}{8}$	4.86 $\frac{1}{8}$ —86 $\frac{3}{4}$
Montreal . . .	\$ to £	4.86 $\frac{3}{4}$	4.88 $\frac{1}{8}$ —88 $\frac{1}{4}$	4.88 $\frac{1}{8}$ —88 $\frac{1}{4}$
Paris . . .	Fr. to £	124.21	124.22—124.26	124.24 $\frac{1}{2}$ —31
Brussels . . .	Bel. to £	35.00	34.89—34.90	34.89—34.90
Milan . . .	Lire to £	92.46	92.80—92.85	92.80—92.85
Zurich . . .	Fr. to £	25.2215	25.19 $\frac{1}{2}$ —25.20	25.19 $\frac{1}{2}$ —20 $\frac{1}{2}$
Athens . . .	Dr. to £	375	374 $\frac{1}{2}$ —375 $\frac{1}{2}$	375.00—375.30
Helsingfors . .	M. to £	193.23	193—193 $\frac{1}{2}$	193—193 $\frac{1}{2}$
Madrid . . .	Pts. to £	25.2215	38.75—39.30	39.20—39.60
Lisbon . . .	Escu. to £	—	108 $\frac{1}{2}$ —108 $\frac{3}{4}$	108 $\frac{1}{2}$ —108 $\frac{3}{4}$
Amsterdam . .	Fl. to £	12.107	12.12—12.12 $\frac{1}{2}$	12.12 $\frac{1}{2}$ —12 $\frac{1}{2}$
Berlin . . .	M. to £	20.43	20.36—20.37	20.36 $\frac{1}{2}$ —36 $\frac{1}{2}$
Budapest . . .	Pen. to £	27.82	27.79—27.83	27.78—27.84
Warsaw . . .	Zloty to £	43.38	43.34—43.38	43.34—43.38
Riga . . .	Lats to £	25.2215	25.24—25.29	25.20—25.30
Bucharest . . .	Lei to £	813.6	817—819	817—820
Constantinople .	Pst. to £	110	1,040—1,070	1,040—1,070
Belgrade . . .	Din. to £	25.2215	275 $\frac{1}{2}$ —276 $\frac{1}{2}$	275 $\frac{1}{2}$ —276 $\frac{1}{2}$
Kovno . . .	Lit. to £	48.66	48 $\frac{1}{2}$ —49	48 $\frac{1}{2}$ —49
Sofia . . .	Lev. to £	673.659	668—675	668—675
Reval . . .	E. Kr. to £	18.159	18.18—18.24	18.18—18.27
Oslo . . .	Kr. to £	18.159	18.18—18.18 $\frac{1}{2}$	18.18—18.18 $\frac{1}{2}$
Stockholm . . .	Kr. to £	18.159	18.11 $\frac{1}{2}$ —12 $\frac{1}{2}$	18.11 $\frac{1}{2}$ —12 $\frac{1}{2}$
Copenhagen . .	Kr. to £	18.159	18.15 $\frac{1}{2}$ —16 $\frac{1}{4}$	18.15 $\frac{1}{2}$ —18.16
Alexandria . .	Pst. to £	97 $\frac{1}{2}$	97 $\frac{7}{16}$ —97 $\frac{9}{16}$	97 $\frac{7}{16}$ —97 $\frac{9}{16}$
Bombay . . .	Per rup.	18d.	1/5 $\frac{3}{4}$ —1/5 $\frac{7}{8}$	1/5 $\frac{1}{2}$ —1/5 $\frac{3}{4}$
Calcutta . . .	Per rup.	18d.	1/5 $\frac{3}{4}$ —1/5 $\frac{7}{8}$	5 $\frac{1}{8}$ —1/5 $\frac{3}{4}$
Madras . . .	Per rup.	18d.	1/5 $\frac{3}{4}$ —1/5 $\frac{7}{8}$	1/5 $\frac{1}{2}$ —1/5 $\frac{3}{4}$
Hong Kong . .	Per dol.	—	1/6 $\frac{1}{8}$ —1/7	1/6—1/7
Kobe . . .	Per yen	24.58d.	2/0 $\frac{1}{2}$ —2/0 $\frac{5}{8}$	2/0 $\frac{1}{2}$ —2/0 $\frac{5}{8}$
Shanghai . . .	Per tael	—	1/11 $\frac{1}{2}$ —2/0	1/11 $\frac{1}{2}$ —2/0 $\frac{1}{4}$
Singapore . . .	Per dol.	2/4	2/3 $\frac{1}{2}$ —1/3 $\frac{3}{4}$	2/3 $\frac{1}{2}$ —1/3 $\frac{3}{4}$
Batavia . . .	Fl. to £	12.107	12.13 $\frac{1}{2}$ — $\frac{1}{2}$	12.12 $\frac{1}{2}$ —13 $\frac{1}{8}$
Manila . . .	Per dol.	24.066d.	2/0 $\frac{1}{8}$	2/0 $\frac{5}{8}$
Rio de Janeiro .	Per mil.	5.899d.	5 $\frac{9}{16}$ —5 $\frac{3}{4}$	5 $\frac{3}{8}$ —5 $\frac{3}{4}$
Buenos Aires . .	Per dol.	47.577d.	42 $\frac{5}{16}$ —42 $\frac{1}{2}$	42 $\frac{1}{2}$ —42 $\frac{1}{2}$
Valparaiso <sup>1</sup> . .	\$ to £	40	39.76	39.76
Montevideo . .	Per dol.	51d.	43 $\frac{1}{2}$ —43 $\frac{1}{2}$	43 $\frac{1}{2}$ —43 $\frac{1}{2}$
Lima <sup>1</sup> . . .	£E to £P	Par	22% prem. <sup>2</sup>	22% prem. <sup>2</sup>
Mexico . . .	Pesos to £	9.76	10.10—10.30	10.10—10.30

<sup>1</sup> 90 days.<sup>2</sup> Nominal.

The above rates were those prevailing prior to the crisis of 1931. For current quotations the student should consult the City page of one of the newspapers mentioned in the text.



elapsed, so that it must compensate itself for the loss of interest by quoting a slightly less favourable rate to its customer. On the other hand, when selling, it receives sterling immediately, but does not have to provide the foreign currency until the cheque is presented. In this case the customer must be compensated for the loss of the use of his money by a slightly more favourable rate of exchange.

By way of example, let us take the T.T. rate, London on New York, quoted in the table on page 617, namely,  $4.86\frac{1}{8} - 4.86\frac{9}{32}$ . Assuming that the allowance for loss of interest is  $\frac{3}{8} - \frac{7}{16}c.$ , and that the bank dealer wants a profit of  $\frac{1}{32}c.$  in the rate, the various rates might be calculated as follows—

	T.T. or Cable Rate	Cheque or Demand Rate
Buying Rate	$4.86\frac{9}{32} + \frac{1}{32}c. = 4.86\frac{5}{16}$ Market T.T. rate + Dealer's Profit	$4.86\frac{9}{32} + \frac{7}{16}c. + \frac{1}{32}c. = 4.86\frac{1}{2}$ Market T.T. rate + Interest + Dealer's Profit
Selling Rate	$4.86\frac{1}{8} - \frac{1}{32}c. = 4.86\frac{3}{32}$ Market T.T. rate - Dealer's Profit	$4.86\frac{1}{8} + \frac{3}{8}c. - \frac{1}{32}c. = 4.86\frac{1}{2}$ Market T.T. rate + Interest - Dealer's Profit

In addition to the quotation for cheques and sight drafts, further quotations have to be made in respect of bills of exchange drawn at a certain usance. Originally the term "long rate" denoted the rate of exchange applied to such bills at a fixed usance, but it now relates to any bill having more than a few days to run. The term "*Tel Quel*" rate is also applied to an exchange rate calculated in respect of a bill of which part of the usance has already expired. In buying such bills, the dealer must make allowance for the following matters—

(1) Loss of interest on his outlay at the rate of discount ruling in the overseas centre upon which the bill is drawn.

(2) The cost of any foreign bill stamps, taxes, agent's collecting charges, etc.

(3) An allowance for his own profit.

By way of illustration, let us consider the following example. A London dealer is asked to quote a competitive rate for the purchase from a customer of a 90 d/d bank bill on San Francisco for £3,472.50. The London Exchange Market quotes T.T. New York as  $£4.86\frac{1}{8} - \frac{1}{4}$  per £, while there is a charge of  $\frac{1}{16}c.$  per £ for transfers of funds from San Francisco to New York. If the discount rate for the proffered



bill is 3 per cent per annum in New York, what would be the best rate for the customer which the London dealer could quote? (Take 360 days to the year, allow  $\frac{1}{100}$  c. per £ profit for the London dealer, and ignore stamps and expenses.)

T.T. Buying Rate . . . . .	\$4.8625
Interest = $\frac{4.8625 \times 3 \times 90}{100 \times 360}$ . . . . .	036469
Transfer Charge . . . . .	.000625
Profit . . . . .	.000625
	<hr/>
	\$4.900210
	<hr/>

The finest rate the dealer could quote would be \$4.90 $\frac{1}{64}$  per £.

**FLUCTUATIONS OF EXCHANGE RATES.**—Although the Mint Par of Exchange gives us a basis for the calculation of exchange rates we find that, in practice, dealing seldom takes place at this rate, but that the exchanges fluctuate about the Mint par. Under an effective gold standard, the amplitude of these fluctuations is restricted to the limits of the gold points, but when a currency is freed from the gold base, the Mint par loses its significance, and fluctuations are much more violent. An exchange rate is determined by the relationship existing at any time between the demand for and the supply of a particular currency. The factors of demand and supply in respect of the various forms of foreign exchange remittance, are themselves subject to a variety of influences, amongst which may be mentioned the following—

(1) **Trade Conditions.** The necessity for making remittances in foreign currencies arises chiefly from international trade in goods and services. Although we may postulate, in normal times, that such transactions will occur in both directions, their aggregate values will never exactly balance, so that there will be a balance of indebtedness due from merchants in one country to those in another. This will create a demand for the currency of the creditor country and a sale of the currency of the debtor country, so that the value of the currency of the former will appreciate in terms of that of the latter.

(2) **Stock Exchange Operations.** Under this heading we may include investment and speculation in securities of international importance, as well as the raising of loans by one country in another. If England lends money to France or Englishmen buy securities on the Paris Stock Exchange, then French people acquire the right to withdraw



funds from London, which tends to depress the value of the pound against that of the franc. If, on the other hand, the Argentine Government is paying interest on loans contracted in London, there will be a tendency for the value of the peso to fall in terms of sterling.

(3) **Banking Influences.** These include a variety of operations which have had, in recent years, a very considerable influence on exchange rates. Since 1918, the majority of banks with international connections have kept a large proportion of their balances in a liquid form in different financial centres, and have moved them from one centre to another as appeared profitable. Such movements of short-term funds, indeed, played a considerable part in our abandonment of the gold standard in 1931. Under this heading, too, we must recognise the influence of arbitrage operations; that is, the buying and selling of foreign currencies by the banks with the object of making profits out of the differences existing between various exchange rates.

(4) **Currency Conditions.** Since the foreign exchange market is concerned with the valuation of one currency in terms of another, any alteration of a currency system within a country tends to have reactions upon the foreign exchanges. Thus, inflationary action by way of an expansion of the note issue or an over-extension of credit has an immediate effect upon foreign exchange rates. Frequently these influences exercise a disproportionate effect upon the exchanges on account of the psychological factor. The mere fact that a currency has depreciated leads people to anticipate still further depreciation, which is reflected in the exchange rate.

(5) **Political Conditions.** The trend of domestic politics, and particularly the budgetary position, are important factors in influencing exchange rates. An unbalanced budget has often been the prelude to currency inflation and financial instability, so that the holders of short-term capital are led to try to increase their security by moving their funds to another centre. Again, the possible accession to power of a body of political thought antagonistic to capital is likely to cause a similar movement. The current industrial position, as revealed by indices of production and employment, exerts a similar influence.

**ELIMINATION OF EXCHANGE RISKS.**—These fluctuations in exchange rates are a considerable source of uncertainty to traders,



since, in the absence of special protection, debtors can never be certain as to their expenses in obtaining the foreign currency necessary to settle their indebtedness. Suppose an English merchant buys from France, on three months credit, goods valued at 80,000 francs, when the franc is 80 to £1. At that time, he knows that the cost of the goods in sterling is £1,000, and he will fix his selling price on this basis. If, however, when he comes to settle the debt the exchange rate has moved so that it is 75 francs to £1, then he will have to find £1,066 13s. 4d. This will probably cause him to make a loss on the transaction. Under a gold standard, these fluctuations are narrowly limited, but in the case of inconvertible paper currencies they may be of considerable magnitude. In order to avoid the uncertainty and possible loss arising from these variations, the following devices may be used—

(1) **Exchange Clauses.** These are recognised forms of wording included in sterling bills drawn by creditors in this country in order to ensure that they receive the full amount of sterling, and that any exchange risk is thrown on the foreign drawee. An exchange clause is included in the wording of such bills and fixes the method of arriving at the rate of exchange at which the drawee must settle the bill. The difficulty is, of course, to get the drawee of such a bill to accept such a clause. As an example let us consider the case of one of the best-known of these clauses, namely, "*Exchange as per endorsement.*" A merchant who has drawn a bill in sterling, bearing this clause, will sell it to his bank at the full face value. The bank, on taking the bill, will immediately calculate a *tel quel* rate of exchange so as to reimburse itself not only for the amount of the bill, but also all expenses and its margin of profit. This rate will be included in the endorsement of the bill, and the foreign debtor will have to settle at this rate.

(2) **Forward Exchange.** The most common method of guarding against exchange fluctuations is by the use of the facility known as forward exchange. Under this system, a banker will give a merchant a definite quotation for the purchase or sale of a foreign currency at some future date. Since 1918 there has been considerable development in the technique of forward exchange and the volume of transactions. The principal forward markets are in dollars, French, Swiss, and Belgian francs, and guilders. Forward contracts can be arranged for a fixed date or for an "option date," when the



actual day of delivery is uncertain. In these circumstances the "option" relates to the *time of completion* of the contract, and the currency must be bought or sold by the last date of the option. The normal maximum period for foreign exchange contracts is three months, and although transactions can sometimes be arranged in the major currencies for longer periods, traders cannot rely on this.

(3) **Foreign Currency Accounts.** A firm having numerous dealings in a foreign country may maintain its own current account in local currency with a foreign bank. In these circumstances, all receipts are credited to that account and all local payments are charged against it. Where this arrangement is undertaken there can be no loss in exchange except when the balance is converted to sterling.

**EXCHANGE RESTRICTIONS AND CONTROL.**—The foregoing are attempts made by business men themselves to mitigate the worst consequences of exchange fluctuations. It has frequently happened in the last few years, however, that the Government itself has stepped in and adopted various methods of exchange control with a view to eliminating these movements. The traditional method of regulating the exchange value of a currency on the gold standard was through the bank rate policy of the central bank. When a country's external payments exceeded its receipts, the exchanges moved against it to the gold export point. There was an outflow of gold, leading to a constriction of credit, a rise in interest rates, and a fall in internal prices. If the initial mischief was not too deep-seated this chain of events provided an automatic cure, for rising interest rates attracted fresh funds from abroad, while the fall in prices stimulated exports and checked imports. Thus the exchange rate tended to return to normal.

When a currency is free or inconvertible these checks do not operate, and it must either be left to fluctuate in accordance with the position of the balance of payments or the whims of speculators, or it must be controlled by official action. This control may be exerted through exchange restrictions, which are official measures having as their object the limitation of the freedom of foreign exchange transactions. An example of this is furnished by the system of the nominal maintenance of the gold standard coupled with the restriction and regulation of the exchanges. Under this system, the central bank is still nominally free to sell and export gold, and the



exchanges are still officially quoted at par. The Government, however, obtains legislative powers enabling it to prohibit remittance abroad of funds for certain specific purposes. Again, there may be prohibitions upon the discharge of outstanding indebtedness to foreign creditors. In such circumstances, the money due to the foreign creditor is said to be "blocked" inside the country, and even its employment within the country is often limited.

Instead of mere restriction, we may have Government intervention in the foreign exchange market, and operations are undertaken by the authorities with a view to influencing the exchange rates. This intervention may be either passive or active. In the former case, we have the method of "pegging" the exchanges at a given rate, at which the bank or banks in charge of the operations are prepared to buy or sell any amount of foreign currencies. Thus, the dollar-sterling exchange was pegged by the Government from 1916 to 1919 at the rate of \$4.76½ per £. Active intervention, on the other hand, means that the authorities or their agents take the initiative in operating in the market, thereby seeking to influence the exchange rates. This form of intervention, if efficiently carried out, is one of the least objectionable, since it imposes no hindrance on either trade or financial activities.

This last method of exchange control is the one which has been resorted to by the British Government in the *Exchange Equalisation Account*. This account was created by the Finance Act of 1932 by the issue of £150,000,000 of Treasury Bills, together with £25,000,000 which formed the residue of the old Exchange Account of pre-war origin. In 1933, it was decided to raise the amount of the fund to £375,000,000. Those operating the account are entitled to hold its assets in the form of gold, sterling, or foreign exchange, and to exchange from one into the other at will. According to the text of the Finance Act, the object of the fund was "the checking of undue fluctuations in the exchange value of sterling." There was no thought of preventing any normal fluctuations of sterling.

In 1936 and 1937 the difficulties of the French franc caused the migration of a large volume of French short-term funds to London. In an attempt to prevent this movement from influencing unduly the internal credit position of Great Britain, the Account was obliged to hold a large portion of its resources in the form of gold. In order to provide additional funds to conduct its operations the



Account was increased to £575 million in June, 1937. In September, 1939, all limits to the borrowing powers of the Account were abolished.

### TEST PAPER LI

1. What is meant by the Foreign Exchange?
2. Can you suggest any explanation for the fact that the Bills drawn on London considerably outnumber those drawn by Great Britain on places abroad?
3. A of Calcutta has occasion to make payments from time to time to B of London. Sometimes he forwards B a sterling draft payable in London, and sometimes he accepts a bill in currency drawn by B payable in Calcutta. You are asked to state in each case to whom B will actually make payment, and from whom A will actually receive payment, and to indicate, shortly, how the indebtedness between the two countries created by these transactions is ultimately settled.
4. State fully what you consider to be the advantages to be secured by the use of bills in connection with commercial transactions—
  - (a) When the debtors are resident in this country;
  - (b) When the debtors are resident abroad.
5. What is meant by the Mint Par, Gold Standard, and Legal Tender?
6. A customer instructs you to remit from London to Paris 10,000 fcs. at 81½. Show the sterling cost of the French cheque, allowing 1½ of 1 per cent for your commission and ½ per mille for stamp.
7. Specify the chief causes of fluctuations in the Foreign Exchanges. What special features are shown in the exchanges of—
  - (a) Silver-using countries?
  - (b) Countries with inconvertible paper?
8. What are the principal factors which may cause instability of the foreign exchanges? What measure have been taken by the British Government to minimise this instability since 1931?
9. The sovereign is an alloy of which eleven-twelfths is pure gold, and the rest base metal. If 1869 sovereigns weigh 40 lb. troy, find the number of sovereigns (to three decimal places) contained in 1 troy ounce of pure gold.
10. Distinguish between spot rates, demand rates, and *tel quel* rates of exchange. What do you understand by "forward exchange"?
11. Show how the exchange between London and New York would be affected by (a) a failure of the wheat harvest in England, (b) a financial panic in the United States, (c) a diminution in the tourist traffic between America and Europe, and (d) the repayment of a large amount of England's War Debt to America.
12. The T.T. rate London on New York on 15th Feb. was 5.03 – 05 dol. per £, and the forward margins were: one month ¼ – ½c. discount; two months ½ – 1c. discount; three months, 1 – 1½c. discount. Assuming that a banker is willing to deal at these rates, what rates would he quote to a merchant who wishes to buy 10,000 dol.—
  - (a) For delivery on 15th March;
  - (b) For delivery on 15th May;
  - (c) For delivery up to 15th April at his option;
  - (d) For spot delivery?
13. Describe the objects and the mode of operation of the British Exchange Equalisation Fund.
14. Give (a) the method of quoting, (b) the par of exchange, and (c) the approximate present exchange rate, in relation to the currencies of the following cities: New York, Paris, Berlin, Bombay.



## CHAPTER LII

### THE MONEY AND CAPITAL MARKETS

**FINANCIAL ORGANISATION.**—As the economic system develops in complexity, it becomes increasingly dependent upon its banking and financial organisation. So long as production is carried on for a purely local market the problem of effecting the settlement of trading transactions is comparatively easy of solution. As the distance between the parties increases with the development of international trade, the need for a special organisation to cope with the problems of financial settlement becomes evident. At the same time, too, greater complexity of economic organisation establishes a demand for capital in large quantities, and institutions come into being for the purpose of satisfying this demand. Financial organisation in its modern form, however, developed with the use of credit instruments such as bills of exchange, shares, and bonds. By the use of these devices, the *liquid resources* of a large number of individuals could be concentrated in the hands of a few institutions which, although not the owners, had the power of the free disposal over them. In this way financial institutions have attained a position of first-class importance in modern economic life, with the result that many people now consider that they should be brought under the direct control of the State.

The *functions* which the financial organisation has to discharge has given rise to varying degrees of specialisation in different centres. Consequently, in most developed centres, the following divisions may be recognised—

(1) **The Money Market** which is engaged in short-term financial operations. It includes transactions in what is known as the Call Loan Market, in which funds available only for very short periods are lent out. So far as London is concerned, this section is primarily associated with the market in bills of exchange, that is the discount market. Secondly, it comprises the operations broadly described as commercial banking, which is concerned primarily with the receipt of deposits and with the granting of short-term loans to finance goods in process of manufacture and in the various stages of distribution.



(2) **The Capital Market** is the organisation through which the supply of, and the demand for, new long-period capital is adjusted. The funds which it supplies may take the form of long-term capital for investment in fixed assets or to serve as permanent working capital for a business; alternatively, it may take the form of long-term loans to central and local government authorities. The institutions engaged in this market comprise issuing houses, investment trusts, and finance companies, whilst the commercial banks participate, though to a limited extent.

(3) **The Stock Exchange**, which may be described as a market for transferring the ownership rights in already existing securities. It is an indispensable adjunct to the long-term capital market described above. It provides facilities whereby investors can liquidate their holdings of capital and thereby induces a greater readiness to invest. At the same time the stock exchange organisation facilitates new investment by providing safeguards for the investor by its investigation of new security issues before granting permission to deal in them on the exchange.

(4) **The Central Bank**, which is the principal financial institution of the whole system and controls its activities in the interests of general financial stability. The general characteristics of such an institution, of which the Bank of England is a particular example, have already been discussed, and it operates under varying degrees of Government control. The necessity for a central bank is urgent at the present day, since one of its fundamental duties is that of the control of money and credit. The control of credit is particularly important under existing conditions, since the greater part of financial activity is based upon the use of credit.

Each great financial centre has its own characteristics, which reflect the economic background against which it has developed. Thus, the City of London has hitherto been noted for the facilities given by the *short-term* money market for the employment of home or foreign funds; in the financing of trade and commerce, both home and foreign; and in the issue of foreign bonds, as distinguished from the financing of British industry. In the past, the market has been singularly free from official interference—a fact which has served to mark it out from foreign centres and has contributed in no small measure to its development.

**THE MONEY MARKET.**—This section of the financial organisation



is concerned with dealings in *short-term capital*, and is therefore of considerable importance in the day-to-day finance of business operations. Thus it will be concerned with the provision of working capital for manufacturing enterprises, the finance of commodities in the course of distribution between producer and consumer, and the dealings in the credit instruments which arise from these transactions. It forms a meeting place for those institutions which have short-term funds seeking temporary investment, and those which can put such funds to profitable use and at the same time preserve the requisite degree of liquidity to enable repayment to be made at short notice. The London Money Market has long been recognised as the most comprehensive and highly organised of the world's financial markets. One of the principal reasons for its supremacy lies in the concentration of British banks upon "deposit" as opposed to "industrial" banking. In consequence, London always possesses, from internal sources alone, an abundant supply of floating balances perpetually seeking short-term investment.

The great commercial banks are thus the most important constituents of the market, since they supply the bulk of the commodity in which it deals. Colonial and foreign banks and finance houses also find it profitable to deal in the London money market, and there is usually a large amount of foreign capital from these sources seeking investment. Again, the market may be supplied with funds awaiting permanent investment in the hands of financial institutions, such as the proceeds of loans and sums available in anticipation of dividend requirements. The regular borrowers are the discount houses, and the stock market operators who need funds to enable them to "carry" the bills of exchange or the stocks in which they are dealing. Again, the acceptance houses may occasionally borrow, though they are often lenders. Finally, the Government itself is a large borrower in the market by the sale of *Treasury Bills*.

The following may therefore be said to be the principal institutions of the money market—

(1) **The Commercial Banks.** Under the English system of deposit banking, the capital resources of the joint stock banks are supplied mainly by their depositors. These deposits are to a very considerable extent repayable on demand, and even those deposits which are fixed for a period may be payable on demand by arrangement with the depositor. In consequence, a considerable sum has to be



held in the form of actual cash which earns no revenue for the bank. Over and above this, however, a large proportion of the assets must be kept very liquid, so that if there are withdrawals of cash owing to a shrinkage of deposits, cash reserves may be replenished quickly. The London money market, with its resources for the employment of short-term funds, offers a channel in which this capital may find profitable employment and at the same time be readily available in case of need. The banks cannot afford to hold a balance of idle cash over and above their standard ratio of from 10 to 12 per cent, since they have to allow interest on practically the whole of their deposits and cover their heavy working expenses. They, therefore, lend any surplus cash to the money market for varying periods. Money is lent out fortnightly, weekly, or monthly, according to the position of the bank, whilst money is lent for a few days to the stock-brokers for the fortnightly account. The methods employed by the different banks with regard to these funds vary; some divide the bulk of their funds up into weekly fixtures, some of which are maturing on each day of the week; others prefer to lend on a day-to-day basis. In either case the banker will have at his disposal daily a large sum of money which he can either reinvest in the market or which he can utilise to meet any demands which are made upon him by depositors. Actually, in normal times, the great bulk of these funds are simply reinvested so that they remain at the disposal of the market for an indefinite period. Another class of loan is known as the *over-night loan*, which comprises temporary advances to billbrokers to enable them to take up bills of exchange offered towards the close of the day's business. These loans are automatically repaid on the following morning.

The amount of funds available in the market from day to day varies on account of the practice followed by the principal banks when compiling their weekly accounts. The ten London Clearing Banks publish monthly figures of reserves in cash and at the Bank of England. These figures are the averages of one selected day in each week of the month, and on this day it is the practice of each Clearing Bank to call in a proportion of its loans to the market, returning them the next morning. Again, since by arrangement the clearing bankers spread their making-up over four days of the week, there are only two days when the full amount of loanable credit is actually available. The Macmillan Committee, commenting



upon this practice, likened part of these cash reserves to a stage army, since the same liquid resources do duty four times over in the course of each week. This practice has been condemned, partly because it gives results which are misleading, and partly on account of its disturbing influence upon the market. The practice is justified by the banks on the grounds that it serves as a check to overtrading and helps to preserve the liquidity of the market's resources.

(2) **Acceptance Houses.** These form part of the specialised machinery of the London money market for dealings in bills of exchange. These institutions, in their capacity as acceptance houses, do not make actual advances of money. They only lend their names to their customers in return for a commission, so that the latter may more readily obtain credit on a bill of exchange. Suppose that a merchant in Brazil is going to sell coffee to a dealer in London. The dealer approaches an acceptance house to open a credit for him in respect of the transaction. Upon receiving their consent, the London dealer instructs the Brazilian merchant to draw a bill on the acceptance house for the value of the consignment. In all probability the foreign exporter will sell this bill, with all the shipping documents attached, to a local bank, and the latter transmit it to London, where it is accepted by the acceptance house. The latter will retain the shipping documents and may hand them over to the London dealer against payment of cash, or against his undertaking to place funds at their disposal against the time when the bill falls due for payment. Under this system, therefore, the credit of the acceptance house is interposed between the seller and the buyer, and assists in the development of trade by promoting confidence. Banks and other financial houses would naturally hesitate to deal in a bill of exchange drawn on an unknown foreign importer, whereas they would take without question a bill drawn under authority upon a London acceptance house. For this service the acceptance house charges a commission which varies according to the credit standing of the person who asks for it.

Practically every acceptance house of old standing in this country commenced as a merchant house trading with foreign countries. It was largely through the offices of these merchants that London became the market and distributing centre for such a large number of raw materials and other commodities. Through these merchants the sterling bill became the international currency of the world, and



as a result a considerable part of the shipments of goods between one part of the world and another is financed by bills drawn on acceptance houses and banks in London. This type of business requires considerable experience coupled with a very careful study of world conditions. Since the acceptance houses are specialist, they can transact business which under ordinary conditions might appear risky, but they are justified in taking that risk because of their special knowledge. For the more efficient conduct of their operations the principal acceptance houses have correspondents and affiliations throughout the world. Thus the London house of Lazard & Co., Ltd., has affiliations with Lazard Frères of Paris, which is a French house, and with Lazard Frères of New York. The London house has also founded a connection in Spain and has a branch in Antwerp and in Brussels. In addition to these, the business has hundreds of correspondents in different parts of the world.

While the mere acceptance of a bill does not involve the immediate financing of trade in cash, bills always tend to be discounted in the market in which they are accepted. This has given rise to a criticism that the market is favouring foreign exporters at the expense of British exporters in providing them with cheap acceptance credit facilities. Yet the existence of this business has brought foreign deposits to this country, which are invested in the money market, and these funds may be said to finance the business. Again, in addition to the substantial commissions which London normally earns from the acceptance business, it also brings all kinds of other business owing to the enormous number of connections which are established. It must be remembered, moreover, that these facilities are equally available for British business houses of good standing, though they are not employed as widely as they might be on account of the aversion of many British firms from the use of bills. At the same time the facilities of the market may be abused as when acceptance credits arranged under the guarantee of foreign banks are used for drawing finance bills under the disguise of commercial bills.

(3) **Discount Houses.** These are institutions which purchase bills before maturity for a sum less than their face value, making their profit on the margin. The *discount market* of London consists of three public companies and some twenty private firms, whose annual turnover of bills amounts to a very large total. As already



indicated, the discount market is largely dependent for its resources upon the volume of the funds which the joint stock banks can place at its disposal. By lending funds in this way to the discount market, instead of investing the whole of them in bills directly, the commercial banks gain a number of advantages. They receive a greater degree of security than is the case when they buy direct, because the bills have passed under the searching scrutiny of a specialist in that type of investment. Further, the bills are backed by the credit of the discount houses pledging them as security for the loan, whilst at the same time the lending banker is not concerned with variations in the capital value of the bills. Again, in the London money market, the discount market provides the link between the central bank and the commercial banks. It is the channel through which any additional bank cash required by the banking community is obtained from the Bank of England. Should the commercial banks require to strengthen their cash position, as, for example, when making up their half-yearly accounts, they call in part of their loans to the discount market. The discount houses, however, have these funds invested in bills of exchange and, in order to meet the demands made upon them, are compelled to borrow from the Bank of England on the security of bills of exchange. Since the Bank will only take bills of an approved type, bearing at least two good British names, one of which must be the acceptor, the discount houses have to exercise due discretion in buying bills.

In recent years, and particularly since the 1931 crisis, the *difficulties of the discount market* have increased considerably. In the first place, the inland bill of exchange finds practically no place in the internal trade of this country, since traders prefer to finance their businesses by bank loans or overdrafts rather than by the discount of bills of exchange. Further, the shrinkage of international trade has naturally reacted upon the supply of commercial bills and has further curtailed the volume of paper coming forward for discount. Even prior to the depression, the composition of the market had changed on account of the growth in importance of the Treasury Bill. This has created competition from the joint stock banks, since the "rating" of a Treasury Bill requires no special knowledge or skill such as is needed in the case of a commercial bill. Since 1933, however, the supply of Treasury Bills has also contracted, and now threatens to cause serious embarrassment to



the market. It is true, of course, that the Government should take advantage of low rates of interest to reduce the volume of the floating debt, as represented by Treasury Bills, by funding. The claims of the taxpayer come first, and a large floating debt constitutes a danger to the national finances. At the same time it must be remembered that the discount market is an essential part of our financial machine, and that its loss would entail a serious diminution in the financial prestige of London. Furthermore, if its effectiveness were to be impaired, the Government itself would be likely to experience difficulties in its short-term financial operations, whilst the commercial banks would probably be driven to invest their short-term funds in the stock market—a line of procedure which experience in other centres has shown to be undesirable.

(4) **Bill Brokers.** In addition to the large discount houses, there are several other firms specialising in the discounting of bills, both as principals and as agents. The bill broker may be considered as an agent whose function it is to bring buyer and seller together and not to deal on his own account. This type of dealer is known as a *running broker*, since he goes from bank to bank, finding out the kinds of bills that certain banks wish to buy and the kind that others wish to sell. Thus, the Eastern and foreign banks always have quantities of bills for sale, which they have received from their foreign offices and customers. On the other hand, the commercial banks are constantly on the look out for bills of special types and maturities. A banker always seeks to hold such a portfolio that some bills are maturing every day, so that he will be continually wanting bills of some particular date to fill a gap. The running broker unites these sources of supply of and demand for bills. He is, as a rule, a man of small capital, so that he is unable to carry the bills he buys, but must immediately sell them at a fractional profit—usually  $\frac{1}{32}$  or  $\frac{1}{64}$  per cent per annum.

The larger firms acting as principals as well as agents are of a somewhat higher financial standing. They may be regarded in the light of retail dealers in bills who buy them outright either from the running broker or from merchants, and sell them again to the bankers and other buyers. They have a relatively small capital of their own, and the bulk of their purchases are financed by loans from the banks, secured by their stocks of bills. These brokers do not usually make themselves parties by endorsement to the bills



they purchase, but they usually give a letter of guarantee to the buying bank, undertaking to take up any bills which may be dishonoured.

(5) **Bullion Market.** The fact that practically 75 per cent of the world's gold productions comes from within the British Empire has had a material influence in making the London Bullion Market the most important in the world. The business of the market is conducted by four firms of bullion brokers, whilst, in addition, two other firms operate refining plants. The abandonment of the gold standard by this country in 1931 has not materially affected the market, since business is not subject to official regulation, and the free import and export of gold are unrestricted. When this country was on a gold standard, however, the market quotation for gold was naturally limited to within a fraction of the Bank of England's buying and selling prices. Since 1931, however, the price of gold has mainly been governed by the rate of exchange ruling between this country and those which still remain on gold. Thus, the official buying and selling prices for gold in the United States are \$35 per fine ounce. If, therefore, the exchange rate is £1 = \$5 the basis of the London market quotation would be £ $\frac{3}{5}$  or £7 per fine ounce, though this price would be increased by the costs of conveying the gold to New York.

In the market, one *official price* is fixed daily for both gold and silver, that for gold being fixed at 11 a.m., and that for silver at 1.45 p.m. At these two meetings the whole of the official business of the day is transacted, and orders received before these times are, except on very rare occasions, executed at the official prices. The official quotation for gold is for "spot," and all business is done for cash. Transactions for "forward" delivery are based on the forward exchange rates, but are in no way official. The prices are for fine gold, since most of the gold on offer comes from the refineries and also because the standards of fineness vary from one country to another.

(6) **Foreign Exchange Market.** In every important financial centre there exists a more or less organised foreign exchange market in which foreign currencies are bought and sold. In this section of her financial activities, London's relative importance has increased considerably during the past fifty years, especially since the War. This has been largely due to the fact that, whereas in pre-war days



British traders mainly bought and sold on a sterling basis, much more business is now transacted in other currencies. Since the final abolition of the meetings in the Royal Exchange at the end of 1920, the London market has no central meeting place. Indeed, the market is nothing more than a close network of telephones connecting up dealers and brokers, and spreading out farther by telephone to the provinces and to the nearer Continental centres, and by cable to more distant markets. The actual dealers in the market are the banks and financial houses who maintain foreign exchange departments, numbering over one hundred. No direct business is done among the dealers themselves, but every operation is carried out through the mediation of a broker, of which there are about forty.

The market is now under the joint control of the London Foreign Exchange Bankers' Committee and of a Committee of the London Foreign Exchange Brokers' Association. These bodies, which were originally created after the War, were reconstituted in 1931 at the request of the Bank of England in order to regularise the operations of the market.

The brokers act as intermediaries, bringing buyers and sellers together, and are not allowed to deal on their own account, or to have direct relations with the public. Each broker specialises in one or more groups of exchanges, such as American and Canadian dollars, or French, Belgian, and Italian currencies. The broker does not in any way guarantee the fulfilment of the deals entered into through him, so that at first sight his purpose is confined to linking up existing supply and demand. He may, however, act as an arbiter with regard to the rate agreed upon for each deal. Again, the existence of the broker affords a means of keeping secret the prospective operations of a dealer, since the broker is not supposed to disclose names until the deal has been concluded.

**THE CAPITAL MARKET.**—Under this heading we have to consider that section of the financial organisation which is concerned with the supply of permanent or of *long-term* capital for the use of business enterprise. As already indicated, this market cannot be clearly separated from the short-term capital market discussed above, since in some cases financial institutions operate in both sections. Thus, in the case of the commercial banks, although the nature of their obligations is such that they must keep their assets as liquid



as possible, yet it is well known that they have given considerable assistance to industry by extending long-term capital facilities. Again, the Stock Exchange exists to facilitate the transfer of long-term capital securities, yet much of its business is financed by short-term money market loans. The market, therefore, is by no means clear-cut and definite, and the institutions connected to it shade off into other lines of business. It is composed of a nucleus of institutions engaged principally in raising long-term capital, including issuing houses, trust and finance companies, company promoters, and underwriters. About these we find a much less centralised and organised group, including building societies, insurance companies, solicitors, and others. Moreover, with the exceptions considered below, the English market tends to offer more generous facilities to the large concern of the joint stock company type than to the small business.

The following are the principal institutions of the market—

(1) **Issuing Houses.** The function of the issuing house has been defined by Lavington in *The English Capital Market* as being “to formulate the demand for capital, to present this to the public by the offer of securities, and to facilitate the flow of capital from the public in response.” This work applies not only to capital issues for the purposes of domestic industry and commerce, but also to issues for the benefit of foreign borrowers. In many cases, the *issuing house* purchases the securities which are being issued and re-sells them to the public, thereby assuming a certain amount of risk. This involves a certain warranty of the solidarity of the security and operates as an implied guarantee to the investing public that the proposition has been thoroughly examined and the interests of the investors protected as far as possible. Thus, in the case of an industrial issue, the issuing house has to make an entirely independent examination of the company's position. It should make a study of the industry and the markets in which the company trades; it must use its judgment as to the possibilities of continued prosperity of the concerns along the lines of commercial policy laid down by the management, which includes a study of the uses to which the new capital is to be put. When all these factors have been considered and the scheme has been thoroughly tested, the issuing house can then prepare to make the actual issue. It has on its staff skilled officials whose duty is to study the public taste and



to present to potential purchasers the facts of an issue in the most attractive form.

It was pointed out by the Macmillan Committee that, so far as the London capital market is concerned, a higher degree of organisation is provided in respect of foreign loans than in the case of domestic capital issues. The report emphasised the fact that industry was becoming increasingly internationalised, and that although foreign industrial concerns obtained considerable support from wealthy banking and financial groups, our own industries were at a marked disadvantage in this respect. At the same time, the investor in domestic industrial issues does not receive the protection from exploitation by the unscrupulous which has been accorded to the foreign investor. It has therefore been suggested that the great City issuing houses, which have done so much for British trade in the past by spreading British capital all over the world, might devote some of their unique experience and technique to solving this problem.

(2) **Company Promoters.** The work of the company promoter is somewhat indefinite in character. He may be regarded as a financial intermediary standing between the investor and the business organiser who needs capital for the finance of new inventions, new processes, or reorganisations of industrial structure. When a new company is being formed for the purchase of an existing business or other property, the vendor may assume the functions of the promoter. Again, the work of promotion may be performed by a registered company which is engaged in the formation of a subsidiary or allied business enterprise. Finally, he may be an independent financier who is concerned solely with the profit which he can make by bringing about a successful flotation. In this latter case, in particular, since the promoter has no intention of associating himself permanently with the interests of the new company, his desire to maximise his profit may lead him to over-capitalise the concern. The law attempts to check abuses of the system by insisting upon a full disclosure of all relevant details, and by imposing penalties for false and misleading statements. At the same time, however, it must be recognised that the law cannot afford complete protection to investors unless they are prepared to exercise a certain amount of discrimination for themselves. At its best, the system of company promotion can be of great assistance in



facilitating the flow of capital into industry, but it is notoriously liable to abuse.

(3) **Underwriters.** The function of the underwriter is to guarantee to the promoter that at least a minimum amount of the capital which he is desirous of placing will be subscribed. Under Section 39 (1) of the Companies Act, 1929, in the case of a first allotment of shares, no public company can proceed to allot any of its shares offered to the public for subscription until a minimum amount of the share capital, known as the "minimum subscription," has been subscribed. Moreover, the Fourth Schedule of the Act states exactly what the directors must take into account in fixing this minimum subscription. An issue of shares entails considerable expense, and, if the issue fails, the burden of this falls upon the promoters. Hence, in order to protect themselves, the promoters or the issuing house take out a kind of insurance in the form of underwriting contracts. An underwriting contract has been defined as "an agreement entered into before the shares are brought before the public, that in the event of the public not taking up the whole of them, or the number mentioned in the agreement, the underwriter will, for an agreed commission, take an allotment of such part of the shares as the public has not applied for." The practice of underwriting was introduced in the 'nineties of last century, but it merely superseded and widened the system by which, when an issue was being made, a syndicate was formed with which a sufficient amount was provisionally placed to secure success.

In the case of a large issue, the risk will be too great to be carried by one firm, so that contracts may be made with a number of underwriters. Alternatively, one firm may underwrite the whole issue and then, in order to protect itself, arrange sub-underwriting contracts. In these circumstances, the underwriting commission is passed on to the sub-underwriters, and the principal underwriters retain what is known as an *over-riding commission* for their services.

(4) **Investment Trusts.** These are companies which raise capital and invest it in securities in such a way as to give the best possible income with the minimum of risk. In Great Britain the first trusts were formed in Scotland by groups of individuals—usually co-heirs of large fortunes—who handed over the administration of their funds to a trustee. Resulting from these successful associations, the first investment trust company was formed in London in 1863,



and by 1890 the movement had become popular in both countries. The modern investment trust permits the application of specialised knowledge and skill to the business of investment. This results in the obtaining of a larger yield, combined with greater security of capital and income, than is usually possible to the individual investor, through the principle of diversification. Thus, throughout the depression of 1929-34, the movement as a whole has continued to earn profits. An important feature of these undertakings in this country is the low cost of administration which distinguishes the leading trusts. It is stated that this seldom exceeds  $\frac{1}{8}$  per cent of the company's capital. In the ordinary investment trust, the securities may be changed from time to time under skilled direction. Another type, however, less common in Great Britain, known as the *Fixed Trust* simply holds certain specified shares, but does not change them. The group of securities selected constitutes a unit divided into a given number of sub-units. The purchaser of a given number of sub-units knows that he is acquiring a proportionate share in the block of securities. The selected shares are deposited with trustees who receive all payments by way of dividends, and forward to each holder of sub-units his proper proportion of such payments each half-year.

(5) **Finance Companies.** Certain of these concerns perform work which is similar to that of the investment trusts, except that they tend to specialise in a group of concerns in one industry, and aim at controlling the enterprises in which they are interested. The investment banking houses found in the United States may be classified under this heading. In Germany, again, many of the banks have been compelled to associate themselves closely with industrial development. On account of the scarcity of capital and the lack of investors in the early days of industrial development, the banks were driven to assist industry to obtain permanent as well as short-term capital. When they accepted this responsibility, they were obliged to keep in more intimate touch with the industries with which they had allied themselves. The practical means to this end is the situation of the bank on the boards of industrial and trading enterprises. Thus, the managing directors of the banks are generally on the boards of the most important concerns; the managers are often delegated to the boards of smaller companies; whilst branch managers are nearly always to be found on the boards



of the local concerns in their districts. This relationship commences upon the foundation of the business. Whether it is a case of converting a private firm into a limited company, or of exploiting a new invention by establishing a new enterprise, the assistance of a bank is always invoked. The bank examines the situation and, when necessary, obtains reports from experts. If the bank, after examination, decides to proceed with the scheme, it draws up the plan of financing, determines the amount and the type of capital to be issued, and then, in some cases, itself takes a part of the shares into its security portfolio with the idea of issuing them at a later date.

Such institutions as these, for the purpose of providing *long-term* finance for industry, are almost unknown in this country. Complaints have frequently been made to the effect that many manufacturers desiring to extend their works, and possessors of sound businesses, can make no successful appeal to the ordinary investor, and find themselves cramped through their inability to borrow even relatively small amounts for long periods. This position is largely due to the fact that in pre-War days manufacturers provided new capital for themselves out of their reserves. This was the more easy to do, since many of them operated private family businesses, and therefore it was much more easy to put big profits into reserve than it is where there are a number of shareholders wanting a dividend. Since the War this course of action has in many cases been impossible, and new organisations are needed to cope with the problem. The Macmillan Committee, after commenting on this deficiency in British financial machinery, visualised the foundation of institutions performing the following functions—

- (a) Acting as financial advisers to existing industrial companies.
- (b) Advising in particular as to the provision of permanent capital, its amounts and types.
- (c) Securing the underwriting of and issuing the company's securities to the public, and, if necessary, assisting previously in arranging for the provision of temporary finance in anticipation of an issue.
- (d) Assisting in financing long contracts at home and abroad, or new developments of an existing company, or founding companies for entirely new enterprises.
- (e) Acting as intermediaries and financial advisers in the case of



mergers or in the case of negotiations with corresponding international groups.

**BUSINESS FINANCE.**—Business finance may be defined as the means adopted by business enterprises for raising and administering the funds required to enable them to conduct their operations. At every stage in the life history of the business unit those who are responsible for its direction and management are concerned with questions of finance. From the time when the undertaking comes into existence as a legal entity, and often long before, to the time when it passes out of existence, finance tends to be the dominant consideration in each of its activities. Business finance, therefore, is concerned with such questions as the following—

- (1) The conditions under which a new enterprise may be launched.
- (2) The basis of its capitalisation and the manner in which funds are raised.
- (3) Determination as to when expansion may take place.
- (4) The financing of purchases.
- (5) The financing of production and the control of production costs.
- (6) Determination of the financial aspect of the sales policy in such matters as terms of sale, collections, discounts, and credit.
- (7) The exercise of financial control over every department of the business.

From the foregoing it will be seen that the subject of business finance is co-extensive with the activities of the business itself.

**RECENT DEVELOPMENTS IN INDUSTRIAL FINANCE.**—The prolonged depression in the basic industries of this country revealed the need for a drastic reorganisation of their technical and commercial structure. Yet the depression and a long-continued reduction in demand had caused a widespread failure to earn profits and inability to build up reserves or even to make sufficient provision for depreciation. As the Balfour Committee pointed out in 1929, financial weakness always tends to constitute a vicious circle, since an undertaking or industry whose earnings are insufficient to provide for depreciation and reserves finds great difficulty in keeping its equipment up to date. The more antiquated and inefficient becomes its equipment, the greater becomes the financial weakness and the smaller becomes the possibility of obtaining the fresh supplies of capital which may be the only means of restoring profit-earning



Form of Undertaking	Raising the Initial Capital	Liquidity of the Capital	Sources of Additional Capital	Liability	Direction and Management	Number of Members
I. Sole trading concern.	The initial capital is provided by the founder of the business from his own savings and is represented in his books of account as the difference between the total assets and liabilities on the date of commencing business.	This type of undertaking is cheap and easy to form and the capital may be withdrawn at any time at the will of the owner.	1. Profits may be left to accumulate in the business. 2. Additional investments may be made by the proprietor. 3. Outside resources may be utilised in the form of bank loans and trade credit.	The proprietor is liable for the debts of the undertaking to the full extent of his private estate.	The proprietor himself.	One person.
II. Partnership.	The same as No. 1, except that each partner has his individual capital account.	Relatively cheap and easy to form. The scope and nature of the business can easily be changed if all parties agree.	1. Capital may be provided by all partners to secure the business usually in the form of reserves. 2. As in No. 1. 3. As in No. 2.	Both active and sleeping partners are liable to the full extent of the firm's debts.	Each partner is an agent of the firm and of the other partners, having authority to bind them to any contracts in the ordinary scope of the firm's business.	May not consist of more than twenty partners, or if it is engaged in banking the number is limited to ten.
III. Limited Partnership.	The limited partner invests a specified amount in the firm without incurring an ordinary partner's liability towards the firm's creditors.	The limited partner may, with the consent of the general partners, assign his share.	As in No. 2.	The general partners are liable to the full extent of the firm's debts.	General partners have practically a free hand to conduct the business as they like without the interference of the limited partners.	As in No. 2 except that there must be one or more general partners and one or more limited partners.
IV. Private Limited Company.	Appeal to the public for capital is prohibited.	Transfer of shares restricted.	The limited partner may increase his original investment with the consent of the ordinary partners.	There is a limited liability.	All administrative power is vested in a board of directors, who are elected by the shareholders and must obtain qualification by taking at least one share in the company.	There must be a minimum of two members. The maximum is fifty, exclusive of past and present employees.
V. Public Limited Company.	A general appeal is usually made to the investing public for subscriptions.	The shares are freely transferable.	It is in a better position than any other form of business organisation to obtain fresh capital.	The members are liable only to the extent of the unpaid portion of the shares they hold, or the amount they guarantee to contribute.	As in No. 4.	There must be seven or more members.
VI. Co-operative Retail Society.	Capital contributed by members who are also the customers.	The capital is charged by the admission and withdrawal of members.	1. Through accumulation of reserves. 2. By the admission of new members. 3. By loans from the C.W.S. bank.	The Societies are registered with limited liability under the Industrial and Provident Societies Acts, 1893 to 1928.	Under the direction of a committee of management with the assistance of paid officials.	As in No. 5.



power. There was an urgent need for co-operation between bankers and industrialists in order to assist industrial reorganisation. In order to give a lead in this work the following institutions have been created—

(1) **The Securities Management Trust.** This is a private company formed under the auspices of the Bank of England, which holds the whole of the capital. Owing to abnormal circumstances the Bank acquired certain securities, the possession of which brought it into contact with industry which is no part of a central bank's normal duty. This concern was therefore established to take over this business and conduct it in another building as a matter quite distinct from the Bank's ordinary functions. It must be regarded as a temporary industrial adjunct of the Bank. Its main objects are to advise industry and to examine schemes for reorganisation, to provide in some cases initial capital, or to ensure that schemes are of such a nature as to justify appeals for financial assistance in other quarters. In order to carry through this work, the Trust obtained the full-time services of various experts, technical, accountancy, legal, and labour. The functions of the Trust are mainly consultative and advisory, and it is not intended to form the nucleus of a national credit bank, nor is it an attempt on the part of the Bank of England to enter the field of industrial finance.

(2) **The Bankers' Industrial Development Company.** This company was created in April, 1930, with a capital of £6,000,000. It is a private company and the capital is divided into two classes of shares; £4,500,000 are subscribed by practically all the deposit banks, merchant bankers, and finance houses of the country, and £1,500,000 by the Bank of England. There is a provision that the life of the company is to be for five years only, though it can be prolonged by special resolution. The purpose and policy of the company is to receive and consider schemes for the reorganisation and re-equipment of the basic industries of the country when brought forward from within the particular industry, and, if approved, to procure the supply of the necessary financial support for carrying out the scheme. The initiative must therefore come from the industry itself, and there is no intention on the part of the company to press for reorganisation. The Macmillan Committee suggested that the company should, at a convenient stage, be definitely separated from the Bank of England, since its functions are not appropriate for a



subsidiary of a central bank. In any case, however, the amount of assistance given to industry has not been very extensive.

(3) **Credit for Industry, Ltd.** This concern was formed in 1934 for the purpose of assisting small and medium-sized businesses to raise the capital which they require for expansion. As the Macmillan Committee pointed out, the existing machinery provided by the issuing houses could not be used when the amount of capital needed was small because the expense was too great. The capital of the company is £250,000 to be increased from time to time as required. Additional finance may also be obtained through bank loans or by the issue of debentures and other securities. The company is prepared to provide credit for all types of industry, and in particular for the small and medium-sized undertakings, but it will not finance new inventions or the acquisition of existing businesses. Nor will it compete with the banks or building societies in their specialised fields. The principles of its operation are as follows—

(a) Loans granted may be anything from £100 to £50,000. No loan is too small to consider, but it is not the company's intention to grant individual loans in excess of £50,000.

(b) Loans may be repayable over any period up to twenty years according to circumstances.

(c) The rate to be charged depends on the amount involved, and, to some extent, on the borrower's position and also on the ruling rates for money. In all cases, however, it is probably something less than the rate usually paid on a preference share.

(d) The security depends on the position in each case. It may take the form of a debenture in the case of a limited company in England and Wales, or a mortgage on real or heritable property. Where this is out of the question the company is prepared to consider whatever other type of security may be available.

(e) In granting a loan the company expects the borrower's banker to be in agreement. It has no intention of usurping the functions of ordinary banks.

(f) The company will not interfere with the control of any borrower's business except in the event of a default of a borrower or of his getting into financial difficulties.

(4) **Special Areas Reconstruction Association, Ltd.** This was registered in June, 1936, with a nominal capital of £1,000,000 to assist in the establishment or development of industries in the Special Areas,



Advances are limited to a maximum of £10,000 in the case of any one loan. No capital is subscribed by the State, but assistance is given in the form of a contribution towards management expenses, and of a guarantee against losses of approximately 25 per cent of the total loans made.

**THE BANK OF ENGLAND AND THE MONEY MARKET.**—The Bank of England, in the discharge of its function as a central bank, must control the structure of money and credit of the country in the interests of financial stability. The control of the circulation of legal tender money operates through the provisions of the Currency and Bank Notes Act, 1928. Much more important, however, under modern conditions, is the control of the credit position, which is achieved through what is known as the Bank Rate Policy supplemented by Open Market Operations. Bank Rate may be defined as the minimum rate of discount charged by the Bank to the market for the discount of bills of exchange of an approved type. The type of paper eligible for discount remains at the discretion of the Bank, but its requirements are in practice rigidly fixed. The only bills it will consider are those bearing at least two British names of first-class standing, one of which must be the acceptor. The rate is fixed every week at a committee meeting of the Bank directors held on Thursday, and is communicated to the market. Movements of the rate depend entirely upon the decisions of this committee, in the light of the information at their disposal regarding the financial position and outlook. No explanation of policy is offered to the public—a fact which has given rise to much bitter criticism.

The importance of the Bank Rate lies in the fact that it forms the foundation of all other rates in the market. Thus, the official rate of interest charged by the commercial banks on loans and overdrafts is fixed at about 1 per cent above Bank Rate, with a minimum of from 4 to 5 per cent, whilst the rate of interest which they allow to their customers is about 2 per cent below Bank Rate. At the same time, the rates for call loans and the market rates of discount are also fixed roughly in proportion to it. Hence, a change in the Bank Rate tends normally to cause a change in the entire structure of interest rates in the market. Thus, supposing that the Bank considers that a contraction of credit is desirable, it will take steps to implement this by raising the Bank Rate. At once the joint stock banks will increase their deposit and their loan rates, since if



**Circulation of Money**

*Return of Money out of Circulation* (top left arrow)

*Direction of Money issued by the Bank* (bottom left arrow)

**Entities and Sectors:**

- BANK OF ENGLAND**
- GOVERNMENT (TREASURY DEPT.)**
- JOINT STOCK BANKS**
- BUSINESS UNDERTAKINGS**
- GOVERNMENT (TREASURY DEPT.)** (bottom left)
- INCOME** (table)
- TAXES**
- CONSUMPTION**
- SAVINGS**
- STOCK EXCHANGE**
- MONEY MARKET**
- PRODUCE MARKETS**
- FOR GOODS**
- FOR LOANS**
- FOR SHARES AND DEBENTURES**
- For Government Stocks and Bonds**
- For Bank Deposits**

**Flows and Transactions:**

- Bank of England to Government (Treasury Dept.):** Bills of Exchange, In return for
- Government (Treasury Dept.) to Bank of England:** In return for Documentary Bills
- Bank of England to Joint Stock Banks:** In return for Treasury Bills
- Joint Stock Banks to Bank of England:** In return for
- Joint Stock Banks to Business Undertakings:** For B/E
- Business Undertakings to Joint Stock Banks:** For
- Business Undertakings to Government (Treasury Dept.):** For Public Contracts
- Government (Treasury Dept.) to Business Undertakings:** For Money Borrowed, For Services Rendered
- Business Undertakings to Taxes:**
- Business Undertakings to Consumption:**
- Business Undertakings to Savings:**
- Business Undertakings to Stock Exchange:**
- Business Undertakings to Money Market:**
- Business Undertakings to Produce Markets:**
- Business Undertakings to For Goods:**
- Business Undertakings to For Loans:**
- Business Undertakings to For Shares and Debentures:**
- Business Undertakings to For Government Stocks and Bonds:**
- Business Undertakings to For Bank Deposits:**

**Income Table:**

Official Salaries	Interest on Capital	Wages	Profits
INCOME			

In the diagram the arrows indicate the direction of the flow of currency from the Bank of England through the various channels of the economic system. In return for Treasury Bills, bills of exchange, and other securities, the Bank issues legal tender money, which is used for the payment of taxes, commodities, and for investment; ultimately it returns to the Bank, where it is cancelled after having functioned as a medium of exchange.



they do not raise the former, funds may be withdrawn from their custody to seek more profitable employment. An increase in the deposit rate will tend to attract funds to the bank in order to earn the higher rate of interest, thus preventing them from being employed in other directions. At the same time, those who operate with borrowed money, such as members of the stock market, find that, owing to higher interest rates, their margin of profit is curtailed or wiped out entirely, so that they operate less freely. Discount rates in the money market will also harden, since the discount houses and bill brokers can borrow only on less favourable terms.

The contraction of credit tends to have a deflationary effect upon prices, which show a downward movement. This, in turn, may have the effect of stimulating buying in the home market and so affect the balance of commodity trade. Exports are encouraged whilst imports are checked, and the alteration in the direction of the demand for the means of payment will tend to turn the exchanges in our favour. In any case, the increase in interest rates is likely to attract short-term capital from abroad for investment in London, and this will operate to turn the exchanges in our favour.

Under the operation of a gold standard, the movement of gold in and out of central bank reserves is one guide to Bank Rate policy. If a central bank is losing gold through unfavourable exchanges, the raising of Bank Rate will operate to correct the exchange position and to check the outflow of gold, or even to draw gold from foreign centres to strengthen its reserves. Under existing conditions in this country this index no longer exists. Indeed, for some time now, on account of abnormal conditions, the relationship between Bank Rate and other rates of interest has broken down, and the rate is ineffective. Yet such conditions are purely temporary, and with their passing the Bank rate policy will once more come into its own as a valuable instrument of credit control.

If an increase in the Bank Rate should not have the desired effect in causing credit contraction, the Bank could then resort to the *Open Market* policy. The Bank always holds a large amount of securities as an investment, and quantities of these would be offered for sale in the market. If the Bank were to sell securities in this way, the total of bankers' deposits is decreased, and the joint stock banks are obliged to curtail their advances and raise their rates for



making them. By using this device to reinforce Bank Rate policy, the central bank possesses a most effective means of credit control over the market.

### TEST PAPER LII

1. "The London money market has long been recognised as the most comprehensive and highly organised of the world's financial markets." Why?

2. Enumerate the principal institutions which constitute the London money market. How does the money market differ from the capital market?

3. What is the short loan fund? Describe the work of the institutions in the London money market which are concerned in its use.

4. The requirements of a successful financial centre are said to be: (a) ample capital resources to lend abroad; (b) adequate banking organisation; (c) freedom of the financial market; (d) an investing public willing to acquire and keep foreign securities; (e) a stable currency; (f) a good money market; (g) a good foreign exchange market. To what extent do you consider the City of London fulfils these requirements? Give reasons for your answer.

5. Write brief notes on the following: Underwriters; Investment Trusts; Finance Companies.

6. What is the structure of the "long-period capital market" in England? Bring out clearly the functions of the different agents engaged in the creation and transfer of long period securities. What possibilities of abuse and waste are inherent in the market?

7. What recent developments have taken place in the development of industrial finance? In your answer bring out the function performed by Securities Management Trust, the Bankers' Industrial Development Company, and the Credit for Industry Ltd.

8. From a study of the table on page 641, state the chief methods of financing the business of a sole trader, a joint stock company, and a co-operative society.

9. How does the Bank of England control the structure of money and credit of the country in the interests of financial stability?

10. The Enterprise Engineering Co., Ltd., was incorporated in 1934 with a capital of 10,000 £1 ordinary and 5,000 6 per cent preference shares which were all taken up. The directors expect a very large increase of business during the next few years, and desire to obtain more capital. They possess powers under the memorandum and articles to issue more; but desire your advice (as secretary) as to the best method of securing additional finance.

Draw up your report to the directors setting forth different methods of obtaining this and stating what methods you recommend and why.

11. Give an outline of the purposes served by finance in the realm of commerce. How is the supply of long period capital generally furnished by financiers?

12. Write brief explanatory notes on *four* of the following: Money at call; Treasury Bills; acceptance houses; discount market; over-riding commission; bank rate; open market policy.



## CHAPTER LIII

### THE STOCK EXCHANGE

As an institution, the Stock Exchange is important in itself, as being the central market for the purchase and sale of all kinds of securities, but it is also an interesting example of business organisation.

The Stock Exchange is usually referred to as if there were but one exchange, viz. the London Stock Exchange. There are, however, Stock Exchanges in the capitals of most countries, and there are in this country quite a number of subordinate Exchanges at the chief provincial centres. In a sense, all of these Exchanges work quite independently, being entirely distinct organisations, but, in another sense, they work together just in the same way as other business houses work together, occupying the respective positions of customer and supplying house. In the case of the Stock Exchange, however, they take it in turn to act as customer. On the outermost fringe of all, there are unattached dealers in stocks and shares who belong to no recognised society and are bound by no rules.

**LONDON STOCK EXCHANGE.**—In its existing form, it does not date very far back, having been re-organised in 1886; but it has existed for appreciably over one hundred years, having carried on business on its present site since 1801. It is really a body in the nature of a club more than anything else, and the members become such solely by election, and are liable to be expelled by the Committee of Management for misconduct. An unusual provision, however, which applies to the Stock Exchange is that all the members have to come up for re-election once a year, in March. This applies not merely to the Committee, but to all the members of the Exchange, so that the controlling body is able to keep a distinct hold upon members, and to eliminate those persons who are not of good reputation. The power of exclusion, however, has not been used in modern times to any extent, except on the occurrence of the Great European War in 1914, when it was exercised on a rather large scale in connection with alien enemies. At the outbreak of the war, persons of enemy origin



(i.e. enemies in the strictest sense) could not be members of the Stock Exchange unless they were naturalised British subjects. As a result of the crisis consequent on the declaration of war, the Stock Exchange was closed, so that the controlling body had time to consider this matter; and, when it re-opened in January, 1915, all persons of enemy birth were required to exhibit proof of de-naturalisation of the country of their origin, and were suspended until they had done so. When the elections came round on March 25th, those who were unable to produce de-naturalisation papers were not re-elected as members of the Exchange. Thus, the danger of appointing undesirable persons as members was dealt with effectively and simply.

**Constitution.** Another peculiarity is the method of appointing the Committee, which is re-elected annually. In the London Stock Exchange there are thirty members re-elected, and every member of the Exchange is entitled to vote. If his vote is to be counted, he must give one vote to each of thirty members. If he fills in a paper of more than thirty names, then the voting paper is null and void. Thus, it becomes easier than otherwise for a number of members to get their candidate on the Committee. In practice, this method of voting works out in favour of the small man's interest, as distinct from the powerful interests of the majority, and there are a few surprises at every election. As a whole, this system of election seems to operate very well, and it is unquestionably the best system to meet the particular requirements of the members of the Stock Exchange.

The London Stock Exchange differs from provincial Exchanges in this important respect—that its members are divided into two classes, called brokers and jobbers, in just the same way as the members of the legal profession in England are divided into barristers and solicitors. It is only within recent years that the precise distinction between a broker and a jobber has been accurately observed, but now the regulations are more stringent.

**STOCK-BROKER.** A broker is a member who acts as agent for others in connection with the purchase or sale of shares. He is allowed to act as agent for any member of the general public, or for another member, including a jobber. Ordinarily, his duty is to act for a client who is a member of the public, and he is engaged either to sell to a jobber securities belonging to that client, or to



purchase from a jobber securities which his client is desirous of acquiring. But a broker may act on behalf of another broker, or on behalf of a jobber. The need for one broker to act for another does not seem to be obvious on the face of it. The reason is, to enable the broker on whose behalf he is acting to operate with greater secrecy as to what he is doing for the time being. The need for the broker to act on behalf of a jobber is that jobbers, being competitors, will not usually deal for each other.

**STOCK-JOBBER.** The jobber does not act as an agent, but as a principal. He buys securities which are offered to him, and sells securities of which he is possessed at the time, or which he believes he will be able to buy in time for the date fixed for delivery. He does not necessarily own what he sells, just in the same way as an ordinary trader often books an order for goods which he has not got in stock. Many persons seem to think that it is very wonderful that this should exist in Stock Exchange transactions, although the case is very similar in other branches of trade. The only essential difference is that, in connection with Stock Exchange operations, the rule as to punctual delivery on the appointed date is much more strictly enforced than in the case of other kinds of trade.

Formerly, jobbers used to deal direct with provincial brokers, but now they are not allowed to do so, since a provincial broker cannot possibly be a member of the London Stock Exchange—to be a member, one must practise within a short distance of the Stock Exchange itself. A member cannot even have his office in the West End, and this, perhaps, seems somewhat strange. The idea is that if a good market is to be established, the members must all be together, so as to facilitate free and rapid intercourse between them.

**AUTHORISED CLERK.** A broker's or jobber's staff comprises two groups: those who are engaged in the highly skilled technical work associated with stock and share dealings and general office routine, and those who are concerned with work inside the Stock Exchange. The latter are subdivided into "Authorised" and "Unauthorised" clerks, the former having the authority of his principals to enter into transactions on their behalf, and the latter lacking such authority but engaged in various useful functions connected with his principals' business.



Thus an authorised clerk is a person elected as member of the Stock Exchange to act there on behalf of his principal. No member may employ more than one such clerk.

An unauthorised clerk is one who is permitted to enter the House as a privilege, but is not entitled to act and make bargains on behalf of his principal. Two such clerks may be employed by each member, but no more.

**NATURE OF STOCK EXCHANGE BUSINESS.**—The Stock Exchange has been referred to as a market in securities, and these are loosely known as stocks and shares. Broadly speaking, these may be grouped under two categories—

The *first* consists of a group of securities which represent the loans issued by public bodies.

The British, Colonial, and Foreign Governments, provincial governments, municipal corporations, and all similar bodies raise money from time to time by borrowing. In exchange they give a form of acknowledgment of the indebtedness which has been given in varying degrees, the quality of marketability. Sometimes the acknowledgments are what the law calls negotiable instruments (i.e. they may be passed from hand to hand) and possession is legal proof of ownership. In other cases, the ownership for the time being is registered. If the owner has nothing in his own hands as proof of possession, they are said to be inscribed stocks, and British Government securities and many Colonial Government securities are inscribed stocks. The proof of ownership is the fact that they are registered in the name of the owner in the books of the bank which acts as registrar of the stock.

Other forms of acknowledgment of indebtedness are a sort of compromise between the bearer securities, which are negotiable, and the inscribed stocks. A certificate of registration is sometimes issued to the owner, and this has to be surrendered when it is desired to record a change of ownership in the register of the undertaking. These certificates, although issued to the owners from time to time in this way, are not proof of ownership. Here, the proof of ownership is the registration, as in the case of inscribed stock. But, with regard to registered stock, the certificates have to be handed over to the purchasers of the stock, whereas, in the case of inscribed stock, the seller has an entry made in the books of the registrar, transferring ownership.



In the case of bearer stock, the documents are simply passed from hand to hand without any registration.

These are three different kinds of securities representing local indebtedness. They are not necessarily securities in the business sense of the term (i.e. that they convey any sort of rights such as those of a mortgagee to enforce payment if there should be default).

The *second* main form of securities is in respect of different kinds of capital issued by public companies, however incorporated, whether by special Act of Parliament at home or abroad, or by registration under the law of the country where they are registered. Such companies may, subject to the laws which govern them, issue capital in practically any form. Accordingly, they issue different kinds of shares, whilst some of them issue stock—which, for all practical purposes, is of the same nature as paid-up shares—and sometimes debentures or debenture stock. All these securities may be dealt in on the London Stock Exchange. This does not mean that every conceivable kind of share is capable of being bought and sold there, but that it might be if the conditions were favourable.

It is clearly a great advantage to investors that their investments should possess the quality of marketability, the power of being sold or turned into money at short notice. It is also an advantage to those who seek to raise capital by these securities that they should be able to attach to them the quality of marketability, for the issue can then be made more easily and on more favourable terms.

**Official Quotation.** Generally speaking, almost any kind of security might be dealt in on the Stock Exchange, but there are various ways of dealing in them. For instance, what might be called the highest group in order of marketability are those securities which are officially quoted, that is to say, those securities the prices of which are published on the official list of the London Stock Exchange, which is issued daily and may be purchased by such of the public as care to pay the price for it. Its circulation is not large except among the members of the Stock Exchange, to whom accuracy is of great importance.

In order that securities may be officially quoted, the concern issuing them must comply with certain formalities. It is not necessary here to consider those formalities, since they are altered



from time to time by the Committee. Generally speaking, however, it may be said that with regard to issues for public authorities (i.e. Central or Local Government stocks), a quotation will never be granted in respect of any loan issued by a Government at war with England. This has always been the rule, and, accordingly, the German War Loan could never be quoted on the London Stock Exchange as long as that nation was at war with us. A quotation may also be refused to authorities which have defaulted in the payment of interest; and that is not by any means an uncommon occurrence. Certain American States have no quoted loans in this country, owing to the fact that they have made defaults in the past.

As regards business concerns, the general tendency of the regulations leading up to an official quotation is as follows. It must be a concern of sufficient size to be of public interest, and, usually, the minimum amount of capital upon which a quotation will be granted is £30,000. This does not mean that the company must have a capital of not less than £30,000, but that the class of shares for which a quotation is required must be not less than £30,000.

One of the reasons why it is practicable to quote prices and have a market in a certain class of securities is that there are a large number of such securities in existence all carrying precisely the same rights. If every share had a different right, or different characteristics, as in the case of many commodities, such a quotation could not exist.

So long as there is a reasonable quantity of the security available, there is always a probability of some persons being willing to buy and some willing to sell. Unless such a condition of affairs arises, there cannot be a market in fact, although there may be one in name. It is for this reason that some companies issue shares at a low face value, as in the case of rubber shares issued at 2s. each. In this case, the number of shares created is greater in proportion to the amount of capital issued than it would be in the case of £1 shares. The increased number of shares has a tendency to increase the number of dealings in them. The market price is due to the number of persons willing to buy as compared with the number willing to sell.

The requirements of shares for which an official quotation is desired are—

- (1) The number of shares issued must be of reasonable size.



(2) The particular issue must have been publicly advertised, and at least two-thirds of the amount issued must have been bona fide applied for by and allotted to the public.

The Stock Exchange will not give a quotation for shares which have not been offered to the public but which carry similar rights to those publicly offered. This is the case where a vendor takes ordinary shares in part payment of the purchase price. The quotation of the vendor's shares is delayed as a rule for two years, to avoid the vendor's shares being unloaded prematurely upon the public and also upon the jobber. Accordingly, not only is an official quotation granted in respect of the particular class of share of a particular company, but it also specifies the distinctive numbers of the shares to which quotation has been granted, and shares bearing outside numbers will not be accepted on the Stock Exchange as delivery of what has been bought.

If the opinion is formed on the Stock Exchange that there has been fraud in connection with the issue, there will be no official quotation, although the Stock Exchange takes no responsibility for guaranteeing the respectability of the issue.

Apart from these officially quoted securities, there is now a large number of securities which are dealt in on the Stock Exchange but which are not included in the official list. There is nothing to prevent members of the Stock Exchange dealing in securities which are not on the official list.

**Method of Dealing.** The next point is as to how these securities are, in fact, dealt in. The method adopted by the London Stock Exchange differs from that of the provinces, and is quite different from that pursued in any foreign or Colonial Stock Exchange; that is, in the intervention of the jobber. A broker receiving an order from a member of the public to buy or sell certain shares is under no obligation whatever to execute the order if he does not choose to do so. But, directly he undertakes to do business for a member of the public, he has to incur obligations to other parties to whom he is liable. It is true that, according to law, an agent is not liable for the defaults of his principal, but an agent is responsible for the defaults of an undisclosed principal, and a broker does not enter the Stock Exchange giving the identity of his client. Consequently, the broker becomes personally liable to the other party for those bargains which he enters into on behalf of his



clients. He is not legally liable to his own client for the default of the persons with whom he has dealt on the Stock Exchange, because there he is being employed as agent, and he does disclose to the client the name of the jobber with whom he deals. Although he is under no legal liability if the jobber should fail to carry out the bargain, it would certainly be regarded as an unusual thing for a broker to plead non-liability in such cases. If he were in the habit of doing so, he would not be re-elected the following March, since it would not be done by a reputable firm of brokers. Although they are agents, brokers take the liability of the contracts they enter into, and, accordingly, it is considered that the time to decide whether the business should be done is beforehand.

Suppose a member of the public has instructed a broker to buy certain shares. The broker goes into the market, which is subdivided into groups according to the general nature of the securities. The chief of these are—

(1) The *Consol Market*, where British Government Stock, Indian Government Stock, London County Council Stock, etc., are dealt in.

(2) The *Home Rail Market*, which deals in the securities of railway companies in the United Kingdom.

(3) The *American Market*, which deals in the securities of the United States and Canadian railways, and with a few industrial concerns (e.g. the United States Steel Corporation).

The first step is for the broker to decide mentally to which group the securities which he desires to buy belong. He then makes his way to that part of the Stock Exchange where the jobbers congregate who deal in the particular class of security. In some markets there may be fifty or more jobbers, whilst in securities which are infrequently dealt in there may be only three or four jobbers willing to quote a price. Jobbers may, therefore, be regarded as specialists in certain classes of securities. Some of them deal in a very large number of securities, and others in a comparatively small number. When the jobber is asked by the broker for a quotation, he will state the prices at which he is willing to deal. The broker will not state whether he wants to buy or to sell, and, therefore, the jobber quotes him a double price, say,  $4\frac{1}{16} - \frac{3}{16}$ . This means that the jobber is willing to buy the securities from the broker at  $4\frac{1}{16}$  or to sell them to him at  $4\frac{3}{16}$ . The mentioning of



this price by the jobber operates as an offer to deal either way in a reasonable quantity of stock so long as the offer is promptly accepted. What is a reasonable quantity of stock depends to some extent on the nature of the security, but it will usually be between £100 and £500 of stock as a maximum. If there is any dispute as to what is a reasonable line, the Committee decides the question after hearing the parties, and the Committee's decision is final, because no member can go to law with another member without the leave of the Committee. If the Committee is doubtful, it declines to give a decision, leaving the parties free to resort to law.

The jobber is supposed to quote a serious price and be ready to deal upon it, but he is not expected to quote a price at which he will buy or sell unreasonable quantities, because if he were to be liable to big risks, such as to find 1,000 shares in a company which was seldom dealt in, or if he had planted upon him 1,000 of such shares he would make the price wider, and that would not increase the marketability of securities generally, so that the jobber is protected by putting a reasonable limit on the shares dealt in at the named prices. The price holds good if it is accepted at once. It is no use for the broker to come back to the original jobber after having visited another jobber, for the former would then be able to say that the price had altered in the meanwhile.

Between the above-mentioned prices there is a difference of  $\frac{1}{8}$ , which is, roughly speaking, 3 per cent. Many persons have the idea that this difference represents the jobber's profit. The position is not nearly so simple as that, for, bearing in mind the great amount of business done daily, there would soon be a rapid increase in the number of jobbers. A jobber may quote a certain price at a time when he may not have stock of that kind at all. If he does not know where he can get such securities, he can decline a price, but if he quotes a price he has to take the consequences. If he knows, or thinks he knows, where he can get this stock at  $4\frac{1}{8}$ , he is quite willing to sell at  $4\frac{3}{16}$ . But if he does not know where he can buy at less than  $4\frac{3}{16}$ , it would mean that he would be doing the deal for nothing, if it is a question of his having to sell. On the other hand, if the jobber is very anxious to buy, he might quote a price which will yield him no profit if the broker wants to deal one way, because he is hoping that the broker will have stock which he is anxious to buy. He has always to be thinking of



his book, and the function of the jobber is to undo his business as quickly as he goes along.

Supposing he has no stock at all at the beginning of the day, but he knows where he can get some at  $4\frac{1}{16}$ . If he buys at  $4\frac{1}{16}$  and sells it at  $4\frac{1}{8}$ , he makes a profit. If he does not know where he can get further supplies, he will have to modify his price. Although he has to modify prices with regard to how he stands, he must remember that he is competing with other jobbers, and it is no use doing business if he quotes entirely different prices from the other jobbers. Sometimes there is such a position, that is, two jobbers standing side by side quoting different prices.

The bargain between the broker and the jobber is supposed to be recorded by each at the time, the record being made in a small, pocket-book known as the Bargain Book, carried by each party. Each makes his own memorandum in pencil. In practice, the jobber does not book his bargain at the time, but he books it when he can.

All bargains are checked the following morning, the usual practice being for the clerks in the offices of the brokers to call round at the offices of the jobbers and check them. In the meantime, the parties to the bargain have reported their respective deals, and these are checked. Should there be any discrepancy, the parties who did the deal have to be referred to, and if they cannot arrive at an agreement as to what did actually occur, they will probably split the difference. But if they do not agree to do that, they will have to refer the matter to the Committee, and the Committee decides which of the two parties is right, and what the bargain is which is binding on both of them. It is remarkable how few discrepancies do arise, even in busy times. The kinds of mistakes apt to arise would usually be matters of price. If the prices fluctuate widely, there may be misunderstanding as to what the unit figure was. Mistakes of that kind are usually settled between the parties by splitting the difference. Sometimes the mistake has reference to the quantity of stock dealt in, but that is not a common mistake between the members of the Stock Exchange. It is a much more common mistake between the client and the broker, and sometimes the broker finds that he has bought or sold more stock than the client intended. In this case, if the stock has gone up in value, the probability is that the client will not repudiate the bargain,



but will give instructions for the excess to be sold. On the other hand, if the stock has gone down, he will probably repudiate the bargain as regards the excess. Sometimes the broker will carry the whole loss, and at others the parties will share the loss between themselves.

Brokers and jobbers seem to be happy-go-lucky in the way they halve losses, but it must be remembered that they are watching each other all the time. If the opinion is formed by one party that the other is habitually making unreasonable demands, the former will avoid the latter in the future. Although bargains between members of the House are conducted in this trustful way, there is no exchange whatever of stamped documents between the parties. That is not the case, however, with regard to the broker and the public.

The broker advises the client of the business done to his order by forwarding him a contract recording, as the case may be, that he has bought or sold such and such stock on account of the client. The contract note is stamped, and is then legally binding on the parties.

**The Settlement.** The arrangement of the Stock Exchange provides that the settlement of bargains shall not take place immediately, but that bargains transacted for a given period shall be settled at the end of that period; and the Committee appoints Settling Days, usually fortnightly. The Settlement lasts four days; the first is called "Making-up" or "Contango" day; the second, "Ticket" day, when the brokers' receipts for stocks and shares are delivered; the third, the "Intermediate" day which is utilized for the preparation of documents; and the fourth, the "Settling" day, when delivery is made of money and shares. Those who have bought are required to pay the agreed price for what they have purchased. The duty of the broker in that case is to pay the jobber, and he receives from the jobber a certificate of transfer in the case of a registered stock. This he has to present for registration, and afterwards must forward the Share Certificate to his client. In the case of *inscribed stock*, the broker and the jobber both meet at the Bank of England, and the transfer is there registered in the books of the bank in the name of the client.

In the case of bearer stock, the jobber hands the securities to the broker in exchange for the money.

Here, again, is an example of the trustful nature of the various



members of the Stock Exchange towards each other. Although these securities sometimes amount to very large sums, they are usually handed over in return for a crossed cheque signed by the broker or jobber as the case may be. The receiving party is entitled to demand notes, although this would be an exceedingly unusual thing to do.

So far as the position of the public and the broker is concerned, there is not the same high standard of credit as between broker and jobber. The broker does not hand over securities to his client until he has been paid for them, and he expects to be paid for them beforehand, so that he can pay the jobber without being out of pocket.

**Carrying-over.** In many cases it may not be altogether convenient for transactions to be settled by the actual payment of money on the appointed date. Either party to the transaction has a right to demand a settlement on the proper day, but one of the parties may ask for the transaction to be carried over : that is to say, a client who has bought securities may postpone payment for them ; in the meantime, however, he does not receive delivery of them.

The need for carrying over bargains on the Stock Exchange may legitimately arise under various circumstances. Sometimes, for instance, in the case of registered stock it is found impossible to get the regulation signatures at the right moment. When stock is in joint names and more than one signature is necessary, the risk of getting the signatures is increased. Again, sometimes there are alterations on the transfer forms which have not been properly initialled, and this makes for delay. Similarly with regard to the question of payment. A person may buy stock thinking he might pay for them on a particular date, but may have to ask for an extension of time. These postponements are quite legitimate and have nothing whatever to do with speculative transactions. Taking this subject a stage further, it may be supposed that a person knows that in three or four weeks hence he will be in receipt of moneys available for investment. He forms the opinion that if he waits until that period has elapsed, prices will not be so favourable as if he bought in the present. Under such circumstances, it is perfectly legitimate for the investor to buy while the prices are favourable and arrange with his broker to carry over the bargain until such time as he will be able to pay



for the goods or securities. Business men are constantly doing this with regard to ordinary trade, so that there is no reason why they should not do it with regard to stocks or any other kind of exchange dealings.

Again, a jobber may sometimes find that he is under a contract to deliver stocks, but, on account of some delay, he is unable to do so. It is, therefore, convenient for him to postpone the date of settlement, or he would otherwise have to buy the stocks for cash and pay a higher price for them than if he were granted an additional fortnight in which to find them.

Up to a certain point, these two kinds of persons—those unable to deliver stocks and those unable to pay for them when delivered—will mutually cancel each other, and then the bargains can be postponed to the satisfaction of both parties. In other cases, they can be postponed only by calling someone into the breach who is willing to tide things over, and that is what usually happens.

**Contango.** Suppose, for example, A has bought £1,000 Railway Stock from his broker and it is inconvenient for him to pay for it at the appointed time, so that the transaction is carried over. In such a case, it remains for the broker to find someone who will be willing to advance money on that particular stock, and out of this the account with the jobber is settled. The carry-over operation is then really a matter of the broker borrowing money against stock delivered to him for the person who has agreed to pay. The persons lending under these conditions receive as security for the advance—

- (1) The actual stock which passes into their name ;
- (2) The personal security of the broker ;
- (3) The personal liability of the client.

Hence, in normal times such loans are fairly well secured.

On the loan, the lender is paid interest at such a rate as agreed upon by the broker, who charges a slightly higher rate of interest to his client to cover himself for his trouble and the risk he is undertaking. This charge which the broker makes to his client is known as *Contango*. So far as the client is concerned, he has postponed the date of payment. Later on, when it is convenient for him to pay back the money which has been advanced against the stock, he will take possession of it in his own name.

**Backwardation.** As regards the postponement of transactions



from the opposite point of view, suppose a broker has contracted to sell stock and finds it is inconvenient to deliver at the settlement. In this case, someone has to be found who owns the particular kind of stock and is willing to lend it. He lends the stock and receives money in exchange. The money represents the security that the stock will be returned to him. On the stock being returned, he has to repay the money; but, for the accommodation, he is entitled to such a commission as may have been arranged between the parties. The rate of this commission depends upon circumstances. If the market is short of stock, it will naturally be higher than if there were a plentiful supply of stock. The commission is known as *Backwardation*.

## TEST PAPER LIII

1. What is meant by the Stock Exchange?
2. Explain the organisation of the London Stock Exchange.
3. Distinguish between a stock-broker and a stock-jobber.
4. Into what two categories may Stock Exchange business be divided?
5. What is meant by an Official Quotation on the Stock Exchange?
6. What are the requirements of shares for which an Official Quotation is required?
7. Explain the method of dealing on the Stock Exchange.
8. Explain carefully the following terms—
 

Dealer's turn	Invisible export
Depreciation	Unfavourable exchange
Gold exchange standard	
9. What is meant by the "Settlement" on the Stock Exchange?
10. "Stock Exchanges are the pattern on which markets have been and are being formed." Comment on this statement, with special reference to the qualities of Stock Exchange securities that make them specially suitable for market dealings.
11. Explain carefully the influence of movements in the Bank Rate on the price of securities on the Stock Exchange. How is trade affected by a low Bank Rate?
12. Give a short explanation of the following terms—Jobbers' turn, bull, bear, spot dealings, contango.
13. Classify the chief kinds of business transacted on the London Stock Exchange. What is the Official List, and what are the functions of jobbers and brokers respectively?
14. Do you consider that the Stock Exchange performs a necessary function in the organisation of modern commerce? What criticism or defence would you make of the Stock Exchange speculator?
15. Describe briefly the organisation of the Stock Exchange, and indicate the functions of the two classes of members. What routine must be followed on the sale of the following types of stock: (a) Inscribed Stock, (b) Registered Stock, (c) Bearer Bonds?
16. Mr. James Williams, High Road, Cardiff, instructs Messrs. Stock & Share, The Stock Exchange, London, to sell 50 Imperial Tobaccos. They do so at £6 per share, and send him a Sold Note containing the following items: 50 Imperial Tobaccos at £6 = £300; commission, £3 15s.; contract stamp, 1s. Draw up the Sold Note.



## CHAPTER LIV

### SPECULATION

“SPECULATION” is one of those words concerning the precise meaning of which there is some uncertainty. In the study of commerce, however, it is necessary to attach definite meanings to the terms used, or it will be difficult to avoid giving impressions different from those intended.

In connection with trading operations, there are three distinct grades of speculation—

- (1) Legitimate business.
- (2) Speculation proper.
- (3) Gambling.

These three grades may be regarded as the positive, the comparative, and the superlative degrees respectively.

**LEGITIMATE BUSINESS.**—This does not by any means necessarily mean that one’s operations are entirely without risk, although it might be an advantage if that were the case. The idea of any kind of business being free from all risks is inconceivable, but operations may be said to be conducted on the lines of legitimate business when the risks involved are limited to those risks which are necessarily incidental to that kind of business. As to whether risks are, or are not, incidental to a particular business must be decided in this way. The man who occupies himself with a business which he fails to understand is running serious risks which are not incidental to the business; but the person who makes himself conversant with everything that appertains to the particular form of undertaking in which he is engaged is more or less of a specialist, and is able to meet with ability and equanimity all those risks which it is inevitable that he should come across in the course of his career. He is dealing with problems he understands; and so long as he confines himself to his own class of business, the risks incidental thereto ought not to be overwhelming.

For example, a cotton spinner who buys his cotton forward and sells his yarn under the same conditions is performing a legitimate operation. He is making sure of his profit in advance and is not running the risk of movements in prices which might turn out to



his disadvantage. He is also performing essential services in that he is providing steady work for his workpeople, whilst the operation itself is tending to keep prices stable in his particular market.

**SPECULATION PROPER.**—Speculation, properly so-called, is something which is not altogether disconnected with a person's own business, but is certainly not inseparably bound up with it. The word indicates "looking about." Speculations are those things which a person picks up when travelling about with his eyes open: that is really the meaning of the word. In the course of his legitimate business, a trader may come across opportunities which are not necessarily connected with his own line. If he grasps these opportunities because he thinks they will be advantageous, that is speculation. For instance, it is a speculation when a solicitor invests considerable sums of capital which are, in part, his own, because he learns that certain property is for sale at prices which strike him as being unusually low. Dealing in house property is much more speculative for a solicitor than for a retired builder who has been connected with that occupation. Thus, a speculator knows something about the things in which he deals, although not so much as he ought to know to be able to reap the best advantages.

**GAMBLING.**—On these lines, gambling may be defined as an operation in something of which a person has little, if any, knowledge. He enters into it blindly because he learns that it may prove to be a good thing, or because he sees that other persons have made money in the same way.

Any extensive gambling in any particular direction is a disturbing element in what might, in the ordinary course of events, be a legitimate business. There are, of course, some forms of gambling which, under no circumstances, can be regarded as legitimate business, such as the operations at Monte Carlo.

By observation and knowledge of the affairs with which they are concerned, business men can to a large extent anticipate the probable trend of future events in the matter of supply and demand. They know by experience when prices are likely to rise and likely to fall. It is true these forecasts are not always correct, but business men are able to build up an experience upon these lines which enables them to make a living out of those operations. Speculation disturbs them to some extent, because



persons not connected with their business step in and take part in it. Gambling is a far greater disturbing factor, because, as a rule, if it occurs at all to any observable extent, it will occur to an extent which dominates the situation. The most prudent business man is as prone to be thrown off his bearings by gambling operations as anybody else.

As a rule, an epidemic of gambling is likely to succeed a period of prosperity coupled with low money rates. If there is money awaiting investment, and legitimate investments stand at prices providing somewhat poor yields, there is a temptation to gamble with the money until more favourable opportunities of investment arise; and if the conditions are favourable to gambling, one may be sure that sooner or later gambling will arise. No one can foresee the exact date when it will begin or the exact intensity it will reach, nor the precise form that the mania will assume.

Whether one is dealing with gambling, speculation, or legitimate business, risks are necessarily involved. The business man cannot avoid risks by confining himself to his own class of business that he understands: all that he can do is to limit the risks to those with which he is more or less conversant, so that he is less likely to be taken unawares.

**"BULLS" AND "BEARS."**—Sometimes persons enter into Stock Exchange or Produce Exchange engagements without any intention whatever of completing their bargain. What they propose to do is to carry forward their accounts and then undo their business at a profit. They have reasons for thinking that the particular stock is going to rise or fall in price, so that they will be able to buy or sell at a profit. These transactions are clearly speculative transactions. On the Stock Exchange, they are spoken of as *Bull* transactions and *Bear* transactions respectively. Thus, by persistently bargaining to *sell* stock which he has not got, the "bear" tends to force prices down. On the other hand, the "bull," by engaging to *buy* more than he can pay for, tends to raise prices. When two sets of dealers are operating against each other in the same stocks, the "bear" is frequently at the mercy of the "bull" when "settling day" arrives. By his continual contracts to buy, the "bull" may have got control of all the available stock of that particular kind, so that it is impossible for the "bear" to deliver what he has bargained to sell. Hence,



he is compelled either to acknowledge his inability to deliver or to purchase enough stock to enable him to complete his contract at whatever price he can get it. On the other hand, the "bull" may be the victim when the "bear" has effectually lowered the price of the stock, and may be able to procure what he has contracted to sell at a price some points lower than that at which he sold.

Take an example of such a speculative transaction: On the 1st November, A sells to B for account—which is on the 16th November—Costa Rica Loan at 79 per cent., the market price at the date of sale being  $79\frac{1}{4}$  per cent. This is, in reality, a speculation on the part of A that on or before the 16th November the price of this particular stock will be 79 per cent. or less. If it falls below the agreed price, say, to  $78\frac{1}{2}$ , B has lost, and must then pay A  $\frac{1}{4}$ th (or half a crown per cent.) on the amount of stock for which he bargained. If the stock does not fall so low as the price agreed upon, but stops, say, at  $79\frac{1}{2}$ , A must pay B  $\frac{1}{2}$  (or 10s. per cent.) on the quantity. This is known as paying the *difference*.

It is well to bear in mind, however, that both "bulls" and "bears" do serve a useful function, or they would have been abolished long ago. They help to steady prices.

An investor in a concern becomes very nervous when an adverse year is experienced and little or no dividend is declared, and hasty selling might result in a drop in prices altogether out of proportion to the real value of the shares; with disastrous consequences to the holders, and to the credit of the company. Similarly, artificial inflation might take place with equally disastrous consequences to the buyers of the securities. Bull and bear operations help to steady prices by putting a certain amount of check on violent fluctuations.

When the shares are unduly high, "bear selling" takes place in anticipation of a fall. This acts as a deterrent to artificial inflation, and then, when the reaction sets in and the prices fall, the "bears" cover their transactions by purchasing the shares at the lower prices. Consequently, "bear selling" prevents prices becoming unduly high, and "bear covering," or purchasing, prevents prices becoming ruinously low.

The position of the "bear" is a most difficult one. A very rich man might easily be ruined in undertaking to deliver a



comparatively small amount of stock which cannot be bought. On the other hand, the worst that can happen to the "bull" is that the stock which he has bought may fall down to zero.

**FUTURES.**—There are many kinds of business which are dependent for their success on some one or two raw materials, the annual supply of which is not certain. The cotton industry of England, for instance, is dependent for its prosperity upon the existing supply of raw material, which, in its turn, depends to some extent upon the harvests. In almost every business there will be some factor of supreme importance which determines to a very large extent whether the profits for the year will be exceptionally good or exceptionally bad, or merely average.

Against these exceptionally bad years, one can usually safeguard oneself by some form of insurance. The method of hedging to cover a special risk of this kind is not, as a rule, by effecting a policy of insurance, although that might be practicable if it were the cheapest way to arrive at the result. The cheapest way is very often by buying or selling some staple commodity in advance by what is called operating in "futures."

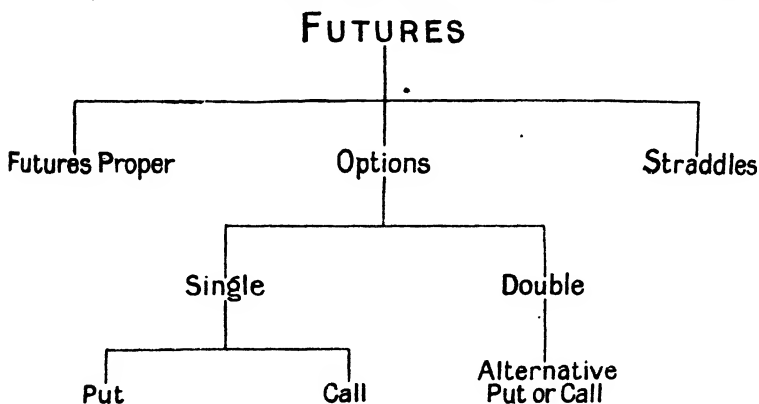
Transactions in "futures" may be regarded, roughly, as a market to enable those who are possessed of commodities which are not capable of immediate delivery to come into contact with those who want to buy, but do not want delivery at once. Instead of the market being limited to the visible stock actually available at a given moment of time, the market covers the general resources of the season. In that way, there is a wider market which tends to be a more satisfactory one, because it is not so subject to fluctuations.

Many persons have the idea that dealing in "futures" in cotton, iron, wheat, or some other commodity, is purely gambling and nothing else. This is not always the case, however. If a manufacturer knows that during the next twelve months he will want to buy a certain number of tons of iron or steel, he may place an order for that quantity now, arranging a part to be delivered at the end of one month, part in three months, and part in six months, etc. Although nominally he is operating in "futures," and although possibly he is buying from someone who has not got the goods to deliver to him, all that he is doing is to buy his goods well ahead of immediate requirements, because the



present price suits him. If he were getting delivery of the goods, it would never occur to anyone that it was not a perfectly straightforward business transaction. What puts a different aspect on the matter is that the goods are not delivered. But, on the other hand, date of delivery is largely a matter of convenience, and it cannot be said to be a part of the purchase or sale of goods that delivery should be immediate. Very often when goods are actually bought and paid for in cash, delivery does not follow immediately, because it is not convenient. Hence, the question of "delivery" is not conclusive in deciding the legitimacy of dealings in "futures."

It is a very common custom in legitimate business for traders to sell goods first, and then buy them afterwards from the sources of supply. The manufacturer will often enter into a contract for the supply of goods at some future date, and at the time he books the order he has not got the goods in stock. Such a transaction would be speculative if he did not know where he could buy them at a price that would suit him, having regard to the price of the goods he has to sell. If he can place orders to cover his liability to deliver goods in the future, there is nothing speculative about the transaction at all. But if he waits until the time when he has to deliver the goods before he buys them, and runs the risk of the market, then that is speculation. When the orders are placed in advance, the manufacturer is avoiding undue risks, and is confining himself to a certain profit instead of an uncertain profit or a large loss. Thus, the business man orders goods ahead of the time when he wants them delivered,





for the sake of avoiding speculative transactions, and is at least keeping within the limits of legitimate trading.

**KINDS OF "FUTURES."**—From the diagram on page 667, it will be seen that "Futures" is a generic term embracing the following—

- (1) Futures Proper      (2) Options      (3) Straddles

In each of these cases, a commodity is purchased or sold which does not really exist, and the speculation is on the difference in price between the time the contract is made and the period when the goods are to be delivered.

**"Futures" Proper.** A "future" transaction is a purchase of goods for delivery at some date in the future at a price settled when the contract is made. Instead of subjecting themselves to the fluctuations of the market, many manufacturers find it expedient to make contracts for future supplies of raw material, and are thus enabled to attend solely to the manufacturing process. In the cotton trade, for instance, the market for the raw material is in the hands of brokers whose business it is to study the "harvest" prospects long before it has been gathered in. Upon their calculations they base the price of "futures." If their calculations prove correct, they will reap a profit, since they will buy the cotton at the future market price and sell it at the present agreed price, which is much higher. The spinner places an order for the delivery of cotton in the future, because—

- (1) He will be sure of having the raw material;
- (2) He must know what to quote to his customers for goods ordered and to be delivered at some later date.

**Options.** These are arrangements to buy or sell a certain amount of commodities at a fixed price within a limited time. If the arrangement is to buy goods, it is known as a "Call Option," whereas a similar arrangement to sell goods is a "Put Option." For this option the person has to pay a price to the broker.

**"CALL" OPTION.** This gives one dealer the option of *buying* from another a certain amount of commodities, at a fixed price, within a certain period. For example, a person anticipating a rise in price of cotton may offer to buy an option to call for, say, 1,000 lb. of raw cotton during the next month at 5d. per lb., the present price being  $4\frac{1}{4}$ d. per lb., and pays 10s. as consideration money. If the market remains unchanged or falls in price before



the end of next month, there will be no profit on the transaction. But if the price of cotton rises above 5d. per-lb., say, to 6d., he can call for 1,000 lb. at 5d. and sell it at the prevailing market price. In this way, he will make a profit of 1d. per lb. less the amount paid for the right to exercise the option. It will, therefore, be seen that by buying a "call" option, the dealer insures against a future rise in the price of a commodity.

**"PUT" OPTION.** This is the reverse of a "call" option. It is the right to *sell* at a fixed price a certain amount of a commodity within a certain period. It is an insurance against the price of the commodity falling. Suppose, for instance, the present price of cotton is  $4\frac{1}{2}$ d. per lb., and a person pays 10s. as consideration money for the option to deliver at any time during the next two months 1,000 lb. of raw cotton at 4d. lb. If the market remains quite steady, or advances, during that period, the option would not be exercised, and the option money would be lost. But if the price of raw cotton fell to  $3\frac{1}{2}$ d. as expected, the 1,000 lb. of cotton would be delivered at 4d. per lb., and the difference, less the option money, would be profit.

**"DOUBLE" OPTION.** This is the right to buy *or* to sell a certain amount of a commodity within a certain period, in the future, at a price fixed in the present. It is an insurance against the market price of a commodity moving either way, since the purchaser can either buy or sell. The amount to be paid for such an option is twice that of a single option, and, in consequence, it is but seldom used.

**Straddle.** This is a speculation on the gaps between the prices of different qualities of a commodity or between the prices of "futures" with different periods to run. For example, suppose a dealer *buys* cotton which is to be delivered in June or July at 5d. per lb., and *sells* the same quantity of "futures" deliverable in July or August at  $5\frac{1}{8}\frac{0}{4}$ d. per lb.; then, whether the prices rise or fall as a whole, he gains, if the difference between the two prices becomes less than  $\frac{1}{8}\frac{0}{4}$ d.; but if it becomes more, he loses. On the other hand, had the dealer *bought* July-August "futures" at  $5\frac{1}{8}\frac{0}{4}$ d. and *sold* June-July "futures" at 5d., he would have gained in the event of the difference increasing, and lost in the event of its decreasing.

**CORNER.**—A "corner" is said to be made when a group of speculators have been able to buy up the whole, or a large portion of the



available supply, of a commodity, and thus force those speculators who have contracted to sell at a fixed price to buy at a high rate from those who have effected the corner.

**HEDGING.**—This may be defined as a device whereby a trader or manufacturer uses the machinery of an organised market for the purpose of protecting himself against loss through fluctuations in the price of the commodity in which he is dealing. An actual sale or purchase of a commodity is balanced against an equivalent purchase or sale for future delivery. The mechanism of dealing in futures, with its utilisation for hedging purposes, enables men to shift speculative risks of price almost entirely to a special class, and this class of speculators takes speculative profits as its compensation for performing this economic service. The market in futures, commonly regarded as exclusively a speculative market, really provides in the hedge an effective means of avoiding speculation.

**MARGIN DEALING.**—This means the purchase of stocks and shares with only a small percentage of the total cost, say, 20 per cent deposited as margin. If £100 worth of stock is bought for a margin of £20, the speculator might sell, say, at £110 and make £10 profit less expenses on his outlay of £20. On the other hand, if the stock dropped to £80, his total margin plus expenses would be lost. This method of dealing is practised largely in the United States and also by bucket shops in this country.

A “bucket shop” is the term used for the office of dealers in stocks and shares who are not members of the Stock Exchange and who generally try to force worthless shares upon the public.

**ARBITRAGE IN GOODS.**—Arbitrage operations in goods and securities are transactions which aim at profiting by the difference of prices existing at a given moment for a certain commodity on different markets.

When a merchant desires to enter into an arbitrage for the purchase of a commodity, he begins by establishing the net parities, or equivalent cost prices in English, of the commodity on the different markets. In calculations of this kind, there are usually two classes of charges to be taken into account: the one comprises the percentage charges, such as commission, insurance, etc., which are dependent upon the amount of merchandise; and the other, the fixed charges—as freight, etc.—which attach to the article without regard to its value.



These parities are then usually arranged in the form of a table as follows—

TABLE OF PARITIES

London . . . . .	23/2
New York . . . . .	23/-
Odessa . . . . .	22/-
Antwerp . . . . .	23/10
Hamburg . . . . .	23/8

From this table it will be seen that it is to the interest of the English merchant to buy at Odessa. If the merchant desires to sell, he chooses the place where the parity is highest.

In the above illustration, this would be Antwerp.

In Stock Exchange dealings, it frequently happens that the same stock is quoted at slightly different prices at the same time in two different places, say, London and Paris. If a slightly higher price rules in Paris, the operator buys in London as much of the stock as he can, and at the same time telegraphs to his correspondent in Paris to sell the same quantity of stock. Hence, if the difference in the prices is sufficiently large, the two operators succeed in making a profit after deducting the necessary expenses. In case the prices were higher in London than in Paris, the operator would sell in London and buy in Paris. In the strict sense, therefore, arbitrage may be defined as a traffic consisting of the purchase, or sale on one Exchange, and the simultaneous, or nearly simultaneous re-sale, or re-purchase on another Exchange, of the same amount of the same commodity.

#### TEST PAPER LIV

1. Distinguish the three different grades of speculation in connection with trading operations.
2. How would you distinguish between "legitimate" and "illegitimate" speculation? Argue the question with reference to some particular market.
3. Point out the distinction between gambling and speculative dealing, together with their respective economic effects.
4. Define "Speculation," and consider how far the speculator performs a useful function in the modern economic system.
5. Explain the uses of "Futures," and indicate any advantages or disadvantages which have followed their introduction.
6. What are futures in cotton? How are they operated? What useful purposes are served by dealings in futures?
7. Copy the diagram on page 667 and explain carefully its meaning.
8. Trace the effect of the introduction of "Futures."
9. What is meant by "Purchasing an Option"?
10. What do you understand by option dealings? Give illustrations of different forms of options, and indicate their function as a means of insurance against adverse price changes.



## ABBREVIATIONS USED IN EXCHANGE, BANKING AND FINANCE

<b>A.</b> . . . Anna (Indian coinage)	<b>Ex in.</b> . . . Without interest
<b>Acc.</b> . . . Acceptance; accepted	<b>E. &amp; O.E.</b> . . . Errors and omissions
<b>A.d. or A/d</b> . . . After date	excepted. These letters are often added
<b>Aff.</b> . . . Affidavit	at the end of an account as a protection
<b>A.P.</b> . . . <i>A protestor</i> (to be protested—bills)	in case of wrong entries in the books
<b>A/S</b> . . . After sight	<b>F/P</b> . . . Fire Policy
<b>Back.</b> . . . Backwardation (Stock Exchange)	<b>H.O.</b> . . . Head Office
<b>B.B.</b> . . . Bill Book	<b>I/I</b> . . . Indorsement irregular
<b>B/C</b> . . . Bills for collection	<b>IOU</b> . . . "I owe you" in an abbreviated form. It is merely a memorandum of a debt
<b>B.D.</b> . . . Bill discounted	<b>I.R.O.</b> . . . Inland Revenue Office
<b>B/D</b> . . . Bank draft	<b>Iss.</b> . . . Issue
<b>B.E.</b> . . . Bill of Exchange	<b>J/A</b> . . . Joint account
<b>Bk.</b> . . . Bank; book; backwardation	<b>L/A</b> . . . Letter of authority
<b>Bkg.</b> . . . Banking	<b>L.C.</b> . . . London cheque
<b>B/L</b> . . . Bill of Lading	<b>L/C</b> . . . Letter of credit
<b>B.N.</b> . . . Bank note	<b>£E</b> . . . pounds, Egyptian
<b>B.O.</b> . . . Branch office	<b>£T</b> . . . " " Turkish
<b>B/P</b> . . . Bill payable	<b>M.C.</b> . . . Marginal credit
<b>B.P.B.</b> . . . Bank Post Bill	<b>M.D.</b> . . . Memorandum of deposit
<b>B/R</b> . . . Bill receivable	<b>M/D</b> . . . Months after date
<b>B/S</b> . . . Bill of sale	<b>M.O.</b> . . . Money order
<b>C/-</b> . . . Coupon	<b>M/S</b> . . . Months after sight
<b>Cap.</b> . . . Capital	<b>n/p</b> . . . Net proceeds
<b>Cash.</b> . . . Cashier	<b>N.A.</b> . . . No advice
<b>C.B.</b> . . . Cash Book	<b>N.a.</b> . . . Non-acceptance
<b>C.C.</b> . . . Continuation clause	<b>N/A</b> . . . New account
<b>C.H.</b> . . . Clearing House	<b>N/E</b> . . . No effects
<b>C/m</b> . . . Call of more (Stock Exchange)	<b>N/F</b> . . . No funds
<b>C/o</b> . . . Cash order	<b>N/N</b> . . . Not to be noted
<b>Consols</b> . . . Consolidated Annuities	<b>N/O</b> . . . No orders
<b>C.P.</b> . . . Charter party	<b>N.P.</b> . . . Notary Public
<b>Cum d.</b> . . . With dividend	<b>N.S.</b> . . . Not sufficient
<b>Cy.</b> . . . Currency	<b>O/D</b> . . . On demand; Overdraft
<b>D/A</b> . . . Days after acceptance; Documents against acceptance	<b>P.N.</b> . . . Promissory note
<b>D/D</b> . . . Demand draft	<b>P.O.</b> . . . Post office; postal order
<b>Dft.</b> . . . Draft	<b>R/D</b> . . . Refer to drawer
<b>Dols.</b> . . . Dollars	<b>Shr.</b> . . . Share
<b>D/P</b> . . . Documents against payment	<b>Sovs.</b> . . . Sovereigns
<b>D/R</b> . . . Deposit receipt	<b>S.P.</b> . . . Supra protest
<b>D/S</b> . . . Day's sight	<b>Spec.</b> . . . Speculation
<b>E/I</b> . . . Endorsement irregular	<b>Stg.</b> . . . Sterling
<b>Exch.</b> . . . Exchange; exchequer	<b>T.M.O.</b> . . . Telegraph money order
<b>Ex ep.</b> . . . Ex coupon	<b>T.t's.</b> . . . Telegraphic transfers
<b>Ex div.</b> . . . Without dividend	<b>x.e.</b> . . . Ex coupon
<b>Ex n.</b> . . . Ex new (without the right of new shares)	<b>x.d.</b> . . . Ex dividend
	<b>x.in.</b> . . . Ex interest
	<b>x.new</b> . . . Ex new



# SECTION VI—TRANSPORT AND INSURANCE

## CHAPTER LV

### MODES OF TRANSPORT

**INTRODUCTION.**—The next important section of Commerce deals with Transport and Insurance. In an earlier chapter, Commerce is defined as *the sum total of those activities which are engaged in the removal of the hindrances of persons, place, and time in the exchange of commodities*. The first of these hindrances is overcome by the advent of the trader as a specialised person, whose duty it is to act as intermediary in effecting the exchange between the producer and consumer. Hence, the personal hindrance is overcome, since there is no longer any necessity for producer and consumer to come into contact with each other. In a similar manner, the hindrance of "*place*" is surmounted by means of Transport and Insurance. Originally, the merchant furnished his own conveyances and supplied horses and men, and looked after the transport himself. Moreover, he built ships and sent them on his own account and risk to the distant parts of the earth. At that time there was no insurance against piracy, theft, fire, and other contingencies. Any accident to the goods in transit might entail an enormous loss to the trader, and sometimes absolute ruin. With the advent of the railway and the steamship, conditions have quite altered. Letters are no longer dispatched by paid messengers, but through a universal and well-organised State Postal Service. Animals drawing their burdens through the main thoroughfares have almost disappeared, and their place has been taken by the locomotive, which has a tenfold greater speed and can convey more goods than countless horses. On the rivers, canals, and inland seas, the restless steam-tug passes from place to place; and giant steamers—capable of carrying enormous quantities of products—traverse the ocean, so that the latter no longer acts as a divider, but as a uniter, of men. Again, if goods are wholly or partially destroyed in course of transit, no



loss is now suffered by the owner, since it is borne by large insurance companies, who recoup themselves out of the premiums paid by the insured. All these and many other facilities have become auxiliaries in the service of trade. Indirectly, it has also called into being the broad roads, and canals, the extensive railways, and the thousand and one shipping lines from and to all parts of the earth. With their increase in complexity, the varying activities connected with transport have gradually separated themselves from trade, just in the same way as banking did in the Middle Ages. Both transport and insurance are now regarded as specialised and independent branches of industry. A large part of the business of transport has been removed from the sphere of private enterprise, and is now conducted as a monopoly in the hands of the State. As instances may be mentioned the postal service; the telegraph and telephone systems; and, in some countries, also the railways and canals.

**GENERAL CONSIDERATIONS.**—The considerations which generally govern the classification of goods for the purpose of fixing the rates of most forms of transportation are—

- (1) The value of the goods.
- (2) The risk of damage.
- (3) The bulk of the goods in proportion to their weight.
- (4) The method of packing and the expenses of handling.
- (5) The regularity and magnitude of the business done.

The relative importance of each of these five considerations differs enormously in different cases. With regard to some commodities, only one or two of these factors come into operation; whilst, in others, practically all of them must be taken into account.

**Value of the Goods.** Railway rates and charges are not determined by the cost of carrying the goods themselves, for if that were the case, some goods would never enter into commerce at all, because their price would not admit of the cost of the carriage. Valuable articles can bear higher rates than cheaper articles. For instance, it would make but little difference in the price of first-class furniture whether the railway company charge £10 or £15 for cost of transport, especially where the total value of the goods amounts to several hundred pounds. The cost of the transport will only be a small item in the total cost of the goods, and will affect the price of the article so little, that the demand



for it will in no way be altered. Further, consignments of valuable goods are relatively few in number, since only a comparatively small number of people can purchase the most expensive commodities. Consignments of such articles as valuable furniture do not take place by the train-load as in the case of coal, and, in consequence, they are more inconvenient to transport. Hence, the rates are higher.

**Risk of Damage.** If damage is incurred by a valuable article, the claim to be met by the railway company is larger than in the case of cheaper goods. The risk of theft is also greater, and a small amount of damage, or theft, might easily absorb the whole of the rate charged. In articles of lower value, the risk is comparatively slight. For instance, if the cost price of coal is 14s. per ton, and a consignment of 100 tons is sent from the Midlands to London at 5s. per ton, it is inconceivable that a claim can be made upon the railway company for damage done to the coal, which claim will absorb more than a trifle of the railway freight.

**Bulk in Proportion to Weight.** Another factor determining the rate to be charged for transporting an article is the bulkiness of an article in relation to its weight. Some articles are extremely light, although they take up a considerable amount of space (e.g. a consignment of straw hats). Again, a consignment of coke is usually twice as bulky as coal. A 10-ton wagon will carry about 10 tons of coal, but only 5 tons of coke.

**The Method of Packing and Cost of Handling the Goods.** The question of good or bad packing influences considerably the amount of risk involved. For instance, cheeses which are well packed will be much less open to risk than those sent loose. The method of packing will also make a difference to the amount carried by each truck. Cheeses packed in wooden boxes can be piled one on the top of the other, whereas those wrapped in cloth can be carried only with difficulty. The method of packing will naturally affect the question of handling. For instance, the difficulty of handling a 10-cwt. consignment of kettles, made up of eight or ten packages of uniform size, is small compared with the same kettles which are sent loose.

In some trades, it is the practice to pack certain grades of goods in particular packages, and the rate charged for conveyance is regulated by the nature of the packing. For instance, in the case



of china goods, cases are used for packing only the more valuable kinds of china, where the breakage of a single article may result in a heavy loss. Second-grade china is usually packed in hampers, whilst the cheapest goods are packed in casks or crates.

**The Regularity and Magnitude of the Business Done.** Throughout the whole of the railway classification of goods, there is frequent reference to the minimum quantities of goods that may be consigned if the lower rates are to be obtained.

Again, take the case of the importation of foreign produce. Danish produce, for instance, is received in this country in good-sized packages, which can reasonably be handled without breakage. Moreover, the wagons are packed as full as possible, the average load being about 5 tons. On the other hand, a different state of affairs exists in regard to home-grown produce—

- (a) A very large proportion of the wagons will contain a ton or less.
- (b) The load may consist of three or four consignments.
- (c) The average load per wagon in an agricultural district is about 30 cwt.

As far as the railway company is concerned, at least three or four wagons must be used for the same quantity of home-grown produce as for the one wagon for the imported products. Hence, it is only natural that the rates for the latter are smaller.

**FORMS OF TRANSPORT.**—The chief forms of transport are—

1. Road. 2. Railway. 3. Canal. 4. Sea. 5. Air.

1. **Road.** Transport by road is probably the oldest branch, and records of road-making and transport by wheeled traffic on roads are of great antiquity. By the end of the eighteenth century, in most civilised countries main roads had been developed to a considerable state of perfection; and horse coach services were well maintained. Even this method, however, was relatively slow, and the condition of side roads generally was still very poor. The application of the steam locomotive in the middle of the nineteenth century to the development of railways stimulated the building of railways all over Western Europe; and from 1850 to 1900, road traffic showed a relative decline.

The invention of the internal combustion engine, however, and its application to road transport at the beginning of the twentieth century, together with the further stimulus applied by War needs from 1914 to 1918, resulted in a great revival of road traffic; this



necessitated road improvements everywhere, and has led to an extensive use of this method of transport for relatively short distances, for passengers and light goods. Other causes of the rapid development of road transport in recent times are—

(1) The congested state of the railways in recent years has caused much delay and created a demand for additional means of transport. Motor transport is very quick and goods can be transported direct to the factory, whereas on the railways they have to be carried on drays from the nearest goods station.

(2) The opening up of new oil wells tends to reduce the price of petrol and hence transport costs.

(3) The great improvement in motor vehicles and in motor transport organisation as a result of the War.

(4) There is no permanent way with elaborate signal stations to be kept up. Taxation, however, is striving to place the burden of road repairs on the transport community.

The limits which may be set to this development seem to be—

(1) The competing railway rates which tend to become lower, and for some goods motor transport will be too costly ; e.g. coal, iron and heavy goods.

(2) The cost of upkeep of the roads and resulting heavier taxation.

For long journeys it would seem that the railways are more favourably placed, but motor transport is excellent for shorter distances and lighter and more valuable articles.

In addition to private individuals who convey their own goods, road transport is conducted by the *Common Carrier*. A *common carrier* is one who carries goods as his regular business, and who holds himself out as ready and willing to do so for any person who may wish to engage him. The consignor may either hire one or more vehicles and load these as he pleases ; or he may deliver separate packages, such as casks, cases, bales, etc., and leave the carrier to complete the load. In some parts, there are brokers whose business it is to bring together such carriers and consignors, and who also undertake to carry for their own account.

There are several kinds of carriers—

(1) **LOCAL CARRIERS**, whose duty is to connect small villages with neighbouring towns.

(2) **RAILWAY CARRIERS**, who act as forwarding agents to the



different railway companies. Among these may be mentioned such firms, as Carter Paterson, Pickford, Sutton, etc.

(3) **SPECIAL CARRIERS**, who restrict their operations to particular trades, such as those in connection with the bonded warehouses, and with the meat and fish trades.

When forwarding goods by a carrier, a receipt is usually obtained on a Delivery Note, or in a Delivery Book specially ruled and printed for the purpose. These receipts should be carefully preserved, as it may be necessary to produce them at some later date, in order to prove delivery of the goods.

The freight charged may be based upon—

(1) A certain weight or measurement ; or for a certain quantity (e.g. 1 cwt., 1 piece, etc.).

(2) On the consignment as a whole (e.g. a full load).

(3) According to a certain fixed tariff (i.e. a charge fixed for a certain distance).

(4) A special arrangement between the carrier and the consignor. Where the carriage has been paid in advance, this is shown on the company's Delivery Note, which is signed by the consignee or his representative.

**II. Railway.** The most important transport by land is that of the railway. From about 1825 to 1845 there was a rapid increase of *Railway Construction* and development. At first it had been intended to charge private vehicles a toll for using the railway line in a similar manner to that in use for roads, but it was seen that the slowest vehicle set the pace, and it therefore became necessary for the railways to take over the whole direction and management and become carriers of goods. By this means large quantities of freight were dealt with at low rates.

In the succeeding period from 1850 to 1890 a period of consolidation on the railways took place. Acts of Parliament were passed dealing with regulation of working, and conditions of land purchase. Land purchase has been the chief factor in railway capital expenditure ; neither shipping nor aircraft having a permanent way to purchase and maintain.

One of the chief of these Acts was the Railway and Canal Traffic Act, 1888, establishing a Commission to deal with technical questions. Until 1900, there was much competition between the various railway companies ; but after a time it was realised that freight



charges could not be economically reduced indefinitely, and working agreements operating over adjacent districts were formulated. This arrangement was continued, broadly speaking, until the outbreak of the War in 1914. After the War, the Railways Act, 1921, provided for the amalgamation of the main line railways; and some 120 separate companies were merged into four groups which have, in turn, developed arrangements for the interworking and the sharing of traffic where their facilities overlap.

In 1840 there were less than 5,000 miles of railways in the world all of which were located in Europe and America. At the present time there are more than 700,000 miles distributed over the various continents. More than two-thirds of this total have been constructed since 1880.

The most rapid development has been in European countries and the United States of America, whilst in the last few decades there has been a noteworthy extension in other parts of the world.

This rapid development of the railway system is due to its superior advantages over other means of transit, such as its speed, cheapness, regularity, and its capacity for conveying huge quantities of goods and large numbers of passengers.

**THE CONSIGNMENT NOTE.** When forwarding goods by rail, a Consignment Note similar to that on page 680 must be filled up. This note is the contract between the consignor and the railway company, and should contain—

- (1) The name and address of the consignor.
- (2) The name and address of the consignee.
- (3) Particulars of the goods.
- (4) Weights and marks.
- (5) Whether at owner's or company's risk.
- (6) Whether carriage is payable by the consignor or the consignee.

The Consignment Note may be made out either at the "Company's risk" or at the "Owner's risk." When the goods are consigned at the latter rate, the railway company is relieved from all liability for damage, mis-delivery, delay, or detention, unless such is caused by the wilful misconduct of the railway company's servants.

**III. Canals.** The first English canal was cut in 1758 by



Pro. No. (3103)

-----Paddington-----Station,-----4 Oct.-----19-----

Signature of Sender or his Representative \_\_\_\_\_ James Brown & Co. \_\_\_\_\_ 42 Church Street, E. C. 3.

**NOTE.**—Goods which may be required "TO WAIT ORDER" at any particular Station must be so consigned on this Note.



Engineer Brindley, who was employed by the Duke of Bridgewater to make water communication between his coal-mines at Worsley and the mills at Manchester. The cost of coal in Manchester, for example, was halved by the construction of this canal. Such was the success of Brindley's scheme, that for the next forty or fifty years canals were constantly being cut, the last decade of the eighteenth century being particularly remarkable for the mania for canal speculation which seemed to have seized capitalists. Shortly afterwards, however, the railways began to develop speed and this factor began to compensate for weight, and traffic on canals declined. Canals had developed so rapidly because most roads of that period were too bad for industrial purposes, haulage was cheaper, and steam had not then been applied to railways, all transport being relatively slow. Although canals have suffered from the competition of railways, there is one class of traffic in which they will probably never be supplanted: this is the transport of bulky articles not worth the expense of railway carriage, such as coal, iron, lime, hardware, or pottery. They cannot, however, be used for such perishable commodities as fruit, fish, or dairy produce. With the exception of some of the smaller canals, where the rates differ little from the railway rates, these are the advantages of transport by canal: loading and unloading at favourable places on route; less risk of loss and damage; practically unlimited capacity for traffic; and cheaper rates.

The Canal Traffic Act of 1888 established the Railway and Canal Commission, under whose authority a uniform classification of merchandise, similar to that adopted for railways, has been made; and uniform maximum tolls and rates have been fixed.

One of the chief drawbacks to canals is that they must always lie on the flat, and inequalities in the ground must be regulated by means of locks, in which vessels can be transferred to a higher or lower level. Sometimes, instead of locks, inclined planes are used, up which the barges are hauled by steam power.

With the development of international commerce, ship canals have begun to play a more and more important part. By means of the Suez Canal, ships bound to and from the East may avoid the long voyage round the Cape of Good Hope. By means of canals, ocean-going vessels are enabled to pass directly from the Atlantic Ocean to the Great Lakes of North America, thus avoiding



the Falls of Niagara. A ship canal enables large ships to sail up to the wharves of Manchester, instead of discharging their cargoes at Liverpool; whilst another canal allows vessels to pass from the mouth of the Elbe to Kiel on the Baltic Sea, without rounding the treacherous shores of the peninsula of Jutland. The Panama Canal forms an alternative route to Australia and the East, and saves the long journey round Cape Horn.

**IV. Sea Transport.** Although railways are important for the transport of goods, they are excelled, however, on the chief commercial highways by the facilities offered by ships. In modern times, the sailing vessel has been supplanted more and more by the steamer; still, on account of the proportionately lower expenses of working, such commodities as saltpetre, copper, phosphate, timber, and sometimes wheat are still transported in bulk by sailing ships. In spite of the long journey, the loss of interest on the merchants' capital is small in comparison with the freights charged by the steamer. This is especially the case in regard to the large modern sailing ships.

Great Britain has for long been the chief maritime power of the world in view of the volume of its overseas trade, which has grown with the growth of the British Empire. Moreover, the Merchant Navy carrying trade received a great impetus from the industrialisation of the country between 1750 and 1850, when England became the factory for the world, and needed an immense mercantile marine to carry products to purchasing countries and import raw materials in return. The continued depression in foreign trade since the War has resulted in a great reduction of these activities. Nevertheless, the long start obtained by Britain in this matter has enabled her to keep ahead of competitors; and the British Mercantile Marine is to-day still the largest in the world.

Lloyd's annual figures relating to the ownership of the world's shipping are shown in the table on page 683 for the years 1914 and 1934, which has reference to motor, steam, and sailing vessels of 100 gross registered tons and upwards.

The table speaks for itself, but it is interesting to notice the growth in the importance of oil fuel, as opposed to coal in the world's shipping. In 1914 nearly 89 per cent of the world's tonnage, even including sailing vessels, was coal driven; in 1935 the figure was less than 60 per cent. The use of oil, meantime, had grown



## MERCHANT SHIPPING OF THE WORLD

Country	1914		1939	
	No.	Tons (000's)	No.	Tons (000's)
Great Britain . . . .	9,240	19,256	7,009	17,894
British Dominions . .	2,088	1,788	2,479	3,321
France . . . . .	1,576	2,319	1,282	2,953
Germany . . . . .	2,388	5,459	2,466	4,493
Japan . . . . .	1,103	1,708	2,337	5,630
Norway . . . . .	2,191	2,504	1,990	4,835
U.S.A. (sea) . . . .	2,490	2,970	2,733	9,336
World Total . . . .	30,758	49,073	31,186	69,440

so rapidly as to account for 38 per cent of the world's tonnage in 1935, as compared with 3 per cent in 1914. Herein, no doubt, lies one of the causes of the depression in the coal industry.

**THE REGISTRATION AND MEASUREMENT OF SHIPS.** The registration of ships is a means of providing a permanent record of a nation's mercantile marine. The owner of a British ship must register it at a port within the British Empire, which is known as the port of registry. When the ownership of the vessel changes hands, this fact must be endorsed on the *Certificate of Registry*. This is a document signed by the Registrar of the port to which the vessel belongs, and usually specifies the name of the vessel, her tonnage, etc.; the name of her master; particulars as to her origin; and names and description of her registered owners. It is the evidence of the nationality and identification of the vessel.

The measurement of ships aims, first, at determining the total capacity of vessels, for upon this is based, to a large extent, the carrying capacity, as well as the port and canal dues which will have to be paid. The total capacity of each ship is officially measured and is expressed in *registered tons*—1 registered ton being equal to 100 cub. ft. The registered (or Board of Trade) ton is, therefore, based upon measurement and not weight. This total capacity of the vessel is known as the *gross tonnage*. The net tonnage is obtained by deducting from this figure the space occupied by the boilers, coal bunkers, and crew accommodation. Every ship has, therefore, two tonnages—a gross and a net.



**CLASSIFICATION.** All ships are not all equally seaworthy. The degree of seaworthiness is, however, of great significance to the consignor of the goods and also to the insurer. According to their seaworthiness, ships are classified. This is effected not by Government officials, but by private companies, such as Lloyd's Register of British and Foreign Shipping in London, the "Bureau Veritas" in Paris, and the Germanic Lloyd in Berlin.

The class into which a vessel is placed is indicated by definite symbols, which differ in each country; but in each case it is an indication of the efficiency of the vessels with regard to their age, construction, and seaworthiness.

**THE SHIP'S MANIFEST.** Every vessel, whether upon an outward or a return journey, must carry a manifest. This is a list of the vessel's cargo, and is usually signed by the shipbroker who clears the vessel out at the Custom House, and by the Master. It must contain—

- (1) The names of the shippers and consignees.
- (2) The marks and number of each separate package.
- (3) A specification of the quantity of goods contained in each package (e.g. rum sugar, etc.).
- (4) An account of the freight corresponding with the bills of lading.

Should the vessel be calling at several ports, the goods for each place must be shown on the Manifest.

**SHIPPING COMPANIES.**—Two-thirds of the ships being built in the world in 1914 were under construction in British shipyards. As soon as the War broke out, sailings from Great Britain were held up because no insurance company would undertake to insure against war risks and owners would not allow their vessels to go out uninsured. The Government, therefore, undertook such insurance itself, and this meant that the Government had to bear the brunt of shipping losses during the War. Until 1920 shipping continued to flourish; then with the commencement of the great depression, the demand for ships declined. This affected all countries, especially the United States. The Americans had built many ships during the War and took full advantage of the war-time demand. By 1921 the Americans, with their high rate of exchange, were unable to compete with other countries. British shipping was also badly hit and ships were sent to lie out in the mouths of rivers. This naturally affected shipbuilding because, if the ships already in existence



could not be used, there was no point in building new ones. Another difficulty was that foreign nations were taking more interest in shipping. For example, there was Japan with her N.Y.K. (Nippon Yusen Kaisha). Italy also went in for shipping; the Greeks bought large numbers of old ships; the Scandinavian countries and France also took a renewed interest in shipping. Germany once more went in for the North Atlantic passenger liners—the *Bremen* and the *Europa*. In the meantime, however, the White Star Line was sold to British interests and finally merged with the Cunard Company.

British shipping to-day can be conveniently regarded by its grouping. The tendency since the War has been for individual companies to combine, and five great groups have resulted, with a few companies still remaining independent.

The five great groups are—

(1) *The Kylesant Group*, which centres round the Royal Mail Steam Packet Company and maintains services to South America, the West Indies, and the North Pacific. Numerous well-known lines are associated with it.

(2) *The Inchcape Group*, of which the Peninsular and Oriental and British India lines are the predominant partners. Both are interested in the Indian, Eastern, and Australian trades, the British India maintaining East African services in addition.

(3) *The Furness Withy Group*, which includes a large number of minor companies for agency purposes, and also a number of important regular lines. Originally its interest was confined almost entirely to the North Atlantic trade, but the activities of the group now extend all over the globe and it possesses some of the finest cargo tonnage afloat.

(4) *The Cunard Group*, which includes the various North Atlantic and Mediterranean services of the Cunard line itself, as well as a number of lines interested in the Australian, New Zealand, and South African trades.

(5) *The Ellerman Group*, which extends its activities all over the globe either by itself or in conjunction with other concerns.

In 1934 the Government gave a subsidy to shipping on condition that the owners of tramp steamers would replace their old ships by new ones. This also assisted the shipbuilding industry. The Government, moreover, granted a loan for the building of the *Queen Mary*. The outlook before British shipping to-day



is better than it has been for several years and shipbuilding is also improving.

**V. Air Transport.** Of increasing significance is the conveyance by aeroplane of passengers, mails, and goods. The enormous development of aviation during the War suggested possibilities of more rapid transport in peace time. A London-Paris Air Mail was introduced in 1919. The result was disappointing, and showed that for short distance services the air service offered little advantage in comparison with the extremely efficient alternative means of land transport. Actually in 1933 the London-Paris service carried little more traffic than ten years before, in spite of an extremely low rate and a very efficient service.

In this country transport by air was somewhat slow in its initial stages. A long distance service naturally involves liberty to fly over all the intermediate countries on the route, and international agreements, which make this possible, took time to negotiate. It became increasingly clear that, without some substantial degree of subsidy, real development of civil aviation was out of the question, and at last, in 1924, a number of separate companies were merged into a single company—Imperial Airways—to which the Government agreed to give a monopoly of government subsidies, and an agreement covering operations for ten years. This agreement was a great landmark in the history of British civil aviation.

At the outset Imperial Airways mainly confined themselves to the development of traffic with Europe, but it became more and more obvious that the real value of air services lay in their use over very long distances, and that, in view of the special conditions of the British Empire, with Dominions and Colonies at distances of from two to twelve thousand miles from the Mother Country, there were great possibilities, political, social, and commercial, in this new and rapid means of communication. Obviously an enterprise such as that of linking up the Empire must be developed by degrees, and on a survey of the position it seemed that the strongest case for the initial experiment was the service between Great Britain and India and thence to Australia. A regular service between Great Britain and Australia was inaugurated at the beginning of December, 1934, the time occupied being about seven days.

In the meantime there has been established another very important Empire extension to South Africa. For some years air surveys



of the route contemplated had been made, and a considerable amount of detailed knowledge was acquired before it became practicable to put on a regular service. There was a choice between the west coast and east coast routes to South Africa; but the balance of advantages seemed in favour of the eastern route, since, with the exception of Egypt, the line of flight would follow British territory throughout. It was also convenient to make a connection at Cairo with the routes to India, and to Australia, and it was clearly economical to run these services over the same route as far as possible.

Air transport excels that by land and water in its greater speed. The improvement in regularity of service during the past few years has been enormous, and the general working of scheduled air services is now so punctual that it can fairly stand comparison with the train and the steamer. Indeed, the aeroplane has become a great time saver, and it is true to say that air transport has now passed from scientific experiment to commercial realisation.

**RESULTS OF MODERN TRANSPORT.**—The great advantage of modern transport is its ability to penetrate inland areas. Before railways were invented, white people did not generally inhabit the interior parts of large continents because of the difficulty of receiving and dispatching goods. This could only be done by native carriers or by rivers. Thus America, Africa, and Australia were inhabited by white people on or near the coasts. When railways came to be built, however, the development of the interior parts became possible. It created new empires with large land masses.

Among the results of the development of modern transport facilities are—

- (1) The sale of heavy and bulky commodities in distant markets.
- (2) The tendency to break down self-sufficiency and to increase territorial division of labour.
- (3) The increased value of Colonial possessions as sources of raw materials.
- (4) The introduction of refrigeration, and the conveyance of perishable goods over greater distances.
- (5) The exploitation of coal and oil resources.
- (6) Increased competition, which in turn has given rise to the formation of pacts and the establishment of combines.

Modern transport provides the conditions for the increased



mobility of passengers and of goods, and thus facilitates trade. At the same time the fear of war has created the desire in most countries to safeguard certain essential services by the erection of tariff barriers. Moreover, railways, steamers, and aeroplanes with their ability to transport human beings and goods on a much larger scale tend to augment the fighting forces and munitions employed in warfare, so that wars are becoming much bigger and more destructive to the nations involved.

### TEST PAPER LV

1. "Transport gives to commodities the utility of being in places where they are required." Discuss this definition, and in the light of your analysis show the influence of efficient transport in a modern community.

2. Enumerate the principal items of development of communication and transport during the past century and remark upon their economic consequences.

3. Enumerate the considerations which govern the classification of goods for the purpose of fixing the rates of most forms of transportation.

4. "Railway rates and charges are not determined by the cost of carrying the goods themselves, for if that were the case, some goods would never enter into Commerce at all." Criticise this.

5. Explain the principle of transport agencies charging "what the traffic will bear," and illustrate some of the effects from the point of view of the trader.

6. Illustrate how the method of packing and the cost of handling goods help to determine the rates of transportation.

7. Agriculturalists in Britain generally complain of unduly high railway rates for agricultural produce, citing as an argument lower rates obtainable on the Continent for similar traffic. Examine the justice of their complaint.

8. Mention three different kinds of carriers, and indicate the nature of their work.

9. Compare the facilities offered by the parcel post with those of the railway.

10. Describe the several ways in which a consignment of hardware goods sold by Messrs. Milward & Co., Ltd., of Birmingham, to Messrs. Phillips & Sons, of Bristol, might reach their destination, paying special attention to the details of the procedure and to the documents involved in the actual act of transport.

11. What is a Consignment Note, and for what purpose is it used?

12. Write short notes upon—

Certificate of Registry;

Net Tonnage; and

Gross Tonnage;

Classification of Ships.

13. What is the object of the Ship's Manifest?

14. Say what you know of the determination of shipping freights?

15. Name some of the chief British Shipping Companies and indicate the sphere of their operations.

16. Enumerate some of the advantages of Canal as compared with other modes of transport.

17. Estimate the significance of air transport.



## CHAPTER LVI

### ROAD TRANSPORT

OF all the forms of transport available in a modern community, road transport is the most recent in its development and the most vigorous in its growth. Although the roads represent the oldest artificial transport medium, the great industrial and commercial development which occurred in this country during the nineteenth century was founded upon the railway as a means of transport. The early years of the nineteenth century were marked by a considerable improvement in the science of road engineering under the influence of such pioneers as Telford and Macadam, but after a short period of development the roads lost their importance for industrial purposes until the *motor car* came into general use in the present century. Hence, at the beginning of the century we possessed in this country an intricate road system of indifferent character, with an infinite variety of width and gradient. The development of mechanically propelled vehicles during the first decade of the century brought with it the need for change and improvement, since roads which were eminently suited for use by the slow-moving horse-drawn vehicle were ill adapted to the heavier and faster motor vehicle.

**GROWTH OF MOTOR TRANSPORT.**—The early experiments in the construction of road vehicles all depended on steam as the motive power, but these were unable to compete effectively against the railways and were, moreover, discriminated by the turnpike trusts, which levied prohibitive tolls upon them. The first stage of the modern development came in 1884 when Daimler constructed the light internal combustion engine, and by 1894 the first petrol-driven motor cars were to be seen on the roads. This new mode of transport met with considerable active opposition, and had to overcome a great deal of prejudice in the mind of the public, and it was not until about twenty years later that the commercial possibilities of motor transport were realised. During the War extensive use was made of the motor transport vehicle, and after 1918 a period of very rapid development began, with the result that our roads are now predominantly used by motor vehicles. The motor vehicle



has transformed the internal transport system of the country, and has completely broken down the former railway monopoly in respect of a wide range of passenger and merchandise traffic. It has given increased mobility to a large section of the population, both for pleasure and for business purposes. Thus, in South Wales, one of the characteristics of the mining valleys has been the isolation to which their inhabitants have been condemned, and the lack of mobility of the people due to the difficulties of inter-valley communication. With the development of road transport, however, this difficulty has been to a great extent surmounted. Inter-valley roads have been constructed at a number of points, and road passenger transport facilities have increased considerably the mobility of the population.

**ADVANTAGES OF MOTOR TRANSPORT.**—The rapid development of road transport, both in the passenger and merchandise branches, has been largely due to certain substantial advantages which it possesses over its competitors. Prior to the development of effective road competition, the great bulk of the internal transport facilities of this country had been provided by the railways which enjoyed a virtual monopoly. One important effect which has emerged from the new conditions is a more lively sense of the need of improvements in rail transport caused by the creation of competition. The railways have been compelled to take measures to bring about an increase in their working efficiency in order to check the inroads which this new form of transport has made upon their revenue. The benefits to the trading public from this tendency are obvious. The following special advantages may be claimed by road transport over competing forms—

(1) **Flexibility.** Road transport has the great advantage over all other forms that, not being tied to a rail or a waterway, it can more easily give a service from point to point without transshipment or breaking bulk. In the case of both canal and railway the vehicles are confined to a certain route, which involves bringing the goods to a terminal either by the customer or by the transport company. In the case of road transport, however, the vehicle can be brought to the point of shipment of the goods and loaded there and then conveyed direct to the final destination. Merchandise can be packed on a lorry exactly as it is desired to deliver it to the customer, as against the numerous handlings entailed by other forms of transport.



Road transport also offers peculiar advantages in the matter of unit consignment, as different parts of the same load can be delivered to various consignees. So far as rail transport is concerned, small unit consignments from the same sender travelling in the same truck will not reap the advantage of the truck-load rate unless the truck is consigned to one individual.

This advantage may be clearly discerned in the case of passenger transport as well. When a person wishes to travel to a particular destination by rail, he may have to go some little distance to the nearest station, and the probabilities are that when he arrives at his destination he will have to make a similar journey. Omnibus routes, on the other hand, are planned to pass the maximum number of points, and although the passenger may not get a "door to door" service, the probabilities are that he will find that the road conveyance gives a much greater degree of convenience. Moreover, upon the development of a new shopping centre or a new housing estate, road transport routes can be extended or modified without difficulties to meet the changing needs of the community.

(2) **Service in Rural Areas.** Road transport services, in respect of both passengers and freight are more readily adaptable than those of the railways. The capital costs of railway construction are very heavy, so that a considerable volume of traffic is necessary in order to make this expenditure worth while. Now, in many rural areas the amount of traffic is not sufficient to make railway operation an economic proposition, with the result that outlying villages are some distance from the nearest railway station and are put to considerable inconvenience when they wish to use the services of the railway. Again, the services which can be provided by the railways in rural districts are usually of a "skeleton" character. The road transport vehicle can overcome these difficulties to a very great extent, since it can select its route in such a way as to pass through all the main villages in the area which it serves. In addition it can, of course, be employed for the conveyance of goods in small amounts as well as passengers. In connection with the marketing of agricultural produce, the Linlithgow Committee pointed out how the use of the motor lorry has facilitated the speedy collection of milk by creameries over a wide area; again, in certain parts of the country live stock are now regularly conveyed direct to market in specially-equipped motor vehicles, where formerly they were either consigned



by rail or driven in on foot. The effect of this development is to extend the producers' markets as well as to effect a reduction in expense.

(3) **Risk of Damage.** One of the most frequent causes of trouble and annoyance to the trading community in the consignment of goods by rail is the necessity for making claims for damage or loss to merchandise. The frequent handling and transshipment, and the fact that goods of all descriptions have to be dealt with, increase considerably the risk of damage, particularly in the case of perishable or fragile goods. For example, in the case of such a commodity as eggs, complaints of breakages on rail are general, and it is a matter of extreme difficulty to apportion the blame between the consignor and the railway company. Claims for compensation in respect of breakages, however, are seldom recognised by the railway companies, as the complainants can seldom show that they have complied with the requirements in the matter of packing. Much of this difficulty can be avoided by using road transport for easily damageable goods. Transshipments are eliminated and economy can be effected in the packing without exposing the goods to such risk of damage. It has been shown, for example, by dealers in glassware and delicate wireless components, that whilst there were breakages in a large proportion of railway consignments, comparatively little damage occurred among goods sent by road.

(4) **Cost of Service.** It is an undoubted fact that one of the features which have done so much to popularise road transport has been the saving made possible to shippers by reason of road transport rates being relatively lower than those for other means of transit. The causes of this difference in cost are complex, and in some cases are subject of keen controversy, but the reduction of rates, both for passengers and freight has been considerable. In some cases the rates quoted by road transport undertakings are one-half those of the railways. In considering some of the causes of this difference it may be noted that the road haulier has fewer expensive obligations than the railway company. For instance, in the matter of safety, the signalling and policing of the roads is done for him by the public authorities at the expense of the community, whilst the railways have been compelled by law to build and maintain an extremely costly and elaborate apparatus which is necessary for the safeguarding not only of the public, but also of their employees. For



this and similar causes in railway operating costs overhead charges which do not vary in relation to the individual job occupy the chief position. In consequence, the basis of railway charges has been commonly described as "what the traffic will bear," and the resultant figure has not necessarily borne any strict relation to actual cost. In fact, to obtain an accurate unit of cost for railway transport is an almost impossible task. The road haulier, on the other hand, has tended to base his rates on actual cost of operation, a basis which is relatively easy to ascertain on account of the relatively small operating units involved, and the fact that direct cost forms the greater proportion of road operating costs.

(5) **Speed of Transit.** So far as relatively short distances are concerned, road transport tends to be quicker than rail on account of the delays caused, in the latter case, by terminal services, collection and delivery, and partly to shunting operations. Short-distance traffic is most affected by this factor, since on the long haul the greater speed of the railway counterbalances these delays. The general advantages of prompt deliveries are obvious, particularly in the case of perishable goods, but a substantial advantage of a less evident type is the more rapid circulation of capital previously locked up in stocks of goods in transit. A typical instance may be cited in the tea trade. Before the introduction of road transport tea was delivered from London to Yorkshire by coastwise steamers, and thence by rail to the inland towns, the time taken being about a week. Now the bulk of this traffic is collected one day by motor lorries in London and delivered in Yorkshire the following day.

**TYPES OF MOTOR TRANSPORT.**—In considering the general economic organisations of the road transport system, we may draw a broad line of distinction between passenger and merchandise transport. Dealing with vehicles in the first class, we have those which are used *privately* and those which are at the disposal of the public and known as *public service vehicles*. The motor vehicles used exclusively for private purposes are private cars and motor cycles, and in recent years, owing to reductions in the cost of production by the application of mass production methods, the popularity of the private car has increased by leaps and bounds. At the present day, indeed, the private car is the most numerous of any class of motor vehicle in Great Britain. It is used extensively both for business and pleasure by large numbers of people, and has



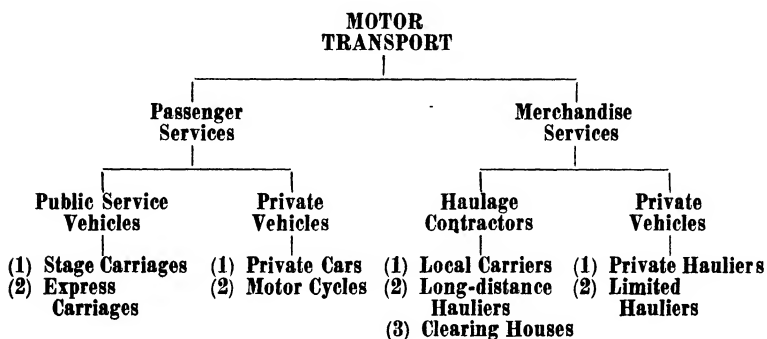
done much to increase the mobility of the population and to spread the travel habit. Professional men, commercial travellers, and other business men make considerable use of the private car, since it renders them independent of other forms of transport and gives them added convenience.

The public service vehicle is one which is used for carrying passengers for hire or reward, the operation of which is regulated under the Road Traffic Acts, 1930 and 1934. Under these Acts, two types of vehicle are distinguished, the first of which is the *stage carriage*. This class of vehicle includes those engaged in local passenger services, operating on the basis of a series of stages, and stopping frequently for the purpose of picking up or setting down passengers. This class of vehicle is engaged mainly on urban and suburban traffic, but it may also connect up near-by towns or a series of villages in a rural area. The second type of vehicle is the *express carriage* which, generally speaking, may be said to be engaged in the conveyance of long distance traffic. In this case stops are made only at certain scheduled points, which are usually at some distance apart. This long-distance road transport is much slower than the railway, but the fare is usually lower and the opportunities of seeing the country are greater for the traveller to whom speed is unimportant.

On the side of goods transport we find a very numerous class of vehicles owned by business houses which employ them exclusively for the purposes of their own business. In much the same category we might place the special vehicles owned by many municipalities for refuse collection, street sweeping, watering, and road construction. On the other side, there is the *haulage contractor*, who is prepared to contract for the conveyance of goods although he has not the obligations of a common carrier. Intermediate between the two is the firm which uses its vehicles mainly for the delivery of its own goods, but is prepared in slack periods to take work under contract for outside firms. In this haulage-contracting business a general line of distinction may be drawn between the long-distance and the short-distance haulier. A long-distance haulier was defined in the Final Report of the Royal Commission on Transport as "a person, firm, or company who is the owner of mechanically-propelled vehicles of any weight, who for his own profit utilises those vehicles for the transport of goods by road belonging to other persons for



distances in excess of thirty miles from the base from which such vehicles operate." This distance of thirty miles is more or less arbitrarily chosen, but for distances between thirty and fifty miles it is possible for the owner of a lorry to make a journey from his point of loading and back in a single day, making due allowance for delays at either end. In such circumstances no special expenses



have to be met for board and lodging of the driver or garage expenses for the lorry, and rates can be kept down to a very low level. Over this limit, however, where a lorry may be away for two or more days, some higher degree of organisation is called for. In the case of the short-distance haulier it is possible to make the return journey empty without suffering any serious loss, but to do so over a long distance must either result in loss to the haulier or cause a substantial rise in freight rates.

**The Public Service Vehicle.** The use of these vehicles, which are engaged in the conveyance of passengers, is governed by the provisions of the Road Traffic Act, 1930. This Act contains comprehensive regulations governing the licensing and control of vehicles used for the conveyance of passengers. Under the term of the Act, England and Wales are divided up into eleven traffic areas, each under the jurisdiction of three Traffic Commissioners. These Commissioners are entrusted *inter alia* with the following duties—

(a) The granting of public service vehicle licences without which no person may allow a vehicle to be employed on the road in that capacity. This licence will not be granted unless the Commissioners are satisfied that the vehicle is of suitable construction and fitness.



(b) The granting of road service licences to operators and attaching suitable conditions to their issue. The decision of the Commissioners as to the granting of a licence will be influenced by such factors as the suitability of the route on which it is proposed to operate, the facilities already in existence, the desirability of the service to the public, and the needs of the traffic area as a whole. It is the aim of the Commissioners to eliminate unnecessary and unremunerative services, and to aim at the co-ordination of all forms of passenger transport, including transport by rail.

(c) The granting of licences to drive or to act as a conductor of a public service vehicle. Before this licence will be granted a driver must produce evidence that he is over 21 years of age and over 18 years of age in the case of a conductor. In either case the applicant must give evidence of his ability to read and write, and produce certificates as to character and physical fitness.

One of the principal tasks of the area Traffic Commissioners contemplated by the Road Traffic Act, 1930, was the elimination of unnecessary services with the object of eventually establishing a "control monopoly" of road passenger transport. As a result of the efforts of the Commissioners a high degree of stability has now been reached in the omnibus and motor-coach industry. The passenger transport industry is now for the greater part under the financial control of a small number of powerful companies, although the various units which comprise it still retain their former names and preserve an outward appearance of independence. There are few concerns which operate networks of omnibus routes outside the large towns whose capital is not held, in part at least, by Thomas Tilling, Ltd., the British Electric Traction Co., Ltd., or their joint holding concern, Tilling & British Automobile Traction, Ltd. In many cases, the interest of these companies is shared by one of the railways, for since the railways were granted powers to interest themselves in road transport in 1928 they have preferred to take an interest in established companies rather than to found new ones.

The Road Traffic Act, 1930, imposed strict regulations with regard to maximum speeds and hours of work for the whole industry. Many of these regulations have been evaded, especially in the road haulage industry, on account of the reluctance of local authorities to add to the many existing duties of the police force. In particular the provisions of the Act with regard to hours of driving has never



been properly observed in the goods transport industry. An attempt is now being made under the Road and Railway Traffic Act, 1933, and also under the Road Traffic Act, 1934, to tighten up these requirements by imposing severe penalties for their infringement and by providing machinery for proper inspection and control.

**Private Fleets of Goods Vehicles.** Of all the motor vehicles engaged in the transport of goods in this country it has been estimated that over 70 per cent are owned and operated by manufacturers and traders for the conveyance of their own products. Under the provisions of the Road and Rail Traffic Act, 1933, the owners of such vehicles are compelled to take out a road service licence—known as a “C” licence—in respect of them. This licence is granted solely upon an undertaking to comply with conditions regarding fitness of the service, speed, and weight limits, hours of driving, and similar matters, and there is no attempt to limit the numbers of such vehicles. As already pointed out, some traders possess their own vehicles which they use primarily for the carriage of their own goods, but are occasionally prepared to carry the goods of other persons. These are known as “limited carriers,” and the Act lays down that such operators must work under licence—known as a “B” licence—and are subject to such restrictions as the Traffic Commissioners may see fit to impose. These restrictions include the following conditions—

- (a) That a vehicle shall be used only in a specified locality.
- (b) That only certain classes or descriptions of goods shall be carried.
- (c) Any other conditions which the commissioners may think fit to impose in the public interest and with a view to preventing uneconomic competition.

In deciding whether a firm shall operate its own fleet of vehicles or hire transport facilities from outside, consideration has to be given to a number of factors. In the first place it must be decided whether the volume of traffic handled is sufficiently large and whether it is of a regular or of a seasonal nature. It is futile to place vehicles on the road if they cannot be employed on a paying basis of operation, that is unless some powerful indirect advantage can be gained from them. Again, before the investment of capital in such a private fleet is made, a careful scrutiny should be made of the maker's



statistics of operating costs, including wages, tax, insurance, depreciation, running costs, and general upkeep, and the unit cost of operation arrived at. This should then be compared with present costs of transport. Finally, a suitable system of organisation must be devised for ensuring proper maintenance and repair, and for keeping a proper record of the movements and work of all vehicles and their drivers.

The possession by a trader of his own fleet of vehicles confers upon him considerable advantages if these are not outweighed by considerations of cost. By owning his own means of transport it is possible for a trader to arrange his deliveries to suit his own convenience or that of his customers—a matter which cannot always be done when he is dependent upon outside firms for transport facilities. Moreover, by keeping the transport of goods under his own control he is enabled to check losses arising from damage or pilferage in course of transit. The driver of a lorry is made responsible for the safe delivery of all goods entrusted to his charge and, in the event of complaints being made by customers, it is possible to assign responsibility for the matter. In any case, on account of the greater personal interest, goods are likely to be more carefully handled by a trader's own employee than by an independent carrier. In recent years, too, there has been a tendency on the part of railway companies to press for more expensive containers and modes of packing in order to facilitate handling. This naturally increases business expenses, whilst friction often arises between the railway and the trader on account of delays in returning empty containers. Where goods are delivered in the trader's own vehicles, packing expenses can be reduced to a minimum. Finally, a private fleet of motor vehicles can be of considerable advertising value to a firm, and there has been a tendency of recent years for firms to order vehicles of special design in order to advertise the products which they are handling.

**The Haulage Contractor.** Under this heading we may include all those organisations whose business it is to carry goods for hire on behalf of the trading public. It is in this section of the motor transport industry that the lowest degree of organisation and the worst working conditions prevail. The Final Report of the Royal Commission on Transport divided road hauliers into three classes, viz.—



- (a) Well-organised companies owning fleets of vehicles.
- (b) Owner-drivers or individuals operating two or three vehicles.
- (c) Clearing houses.

The third of these classes is dealt with later, and for the moment we shall concern ourselves with the first two. The owner-driver is generally a new-comer to the trade and has little business experience, little knowledge of the cost of running a lorry for a series of years, and no appreciable organisation for obtaining traffic. On account of his lack of business capacity and ignorance of costs of operation, he can readily be induced to accept loads at rates which are uneconomic. Moreover, though bankruptcies are frequent amongst this class of operator, entry to the industry is so easy that their places are quickly taken and destructive competition goes on unchecked. A person wishing to enter this trade can purchase a second-hand lorry cheaply or can buy a new one on the instalment system, so that his capital outlay is reduced to a minimum. Amongst this class of operator rates of wages and conditions are poor in the extreme.

An attempt is being made under the *Road and Rail Traffic Act*, 1933, to deal with this overcrowding and unbridled competition in the haulage industry. Under the terms of this Act all public carriers must obtain from the Traffic Commissioners what is termed an "A" licence. A haulier already in business will receive such a licence which is available for two years after the commencement of the operation of the Act. Apart from this exception, however, the licensing authority has discretion to grant licences, and in doing so must take into account objections made by persons already providing facilities for the carriage of goods—whether by road, rail, or otherwise—in the same area as the applicant, together with the general traffic requirements of the area. Further, all licences granted under the Act, including the "B" and "C" licences already mentioned in connection with limited and private carriers, are given subject to the following conditions—

(a) That the vehicle shall be maintained in a fit and serviceable condition.

(b) That the appropriate limits of weight and speed shall be complied with.

(c) That drivers shall comply with the requirements of the Road Traffic Act, 1930, regarding the hours that they may remain on duty.



(d) That records of hours and journeys shall be kept, except where the nature of the business makes it impracticable.

It is hoped as a result of this measure to bring the road-haulage industry to a condition of organisation similar to that prevailing in road passenger transport. Side by side with the owner-driver, well-organised road-haulage companies have always existed, performing service of unquestionable value to the trading public. Their stability has, however, constantly been threatened by the actions of the small owner-driver who has reduced rates to uneconomic levels. It will now be possible, at the discretion of the Traffic Commissioners, to refuse licences to new hauliers where the traffic facilities already available can be shown to be sufficient for the needs of the trading community. In this way, encouragement and a measure of protection will be given to the well-organised company employing an economic scale of rates and charges as against the rate-cutting activities of the small owner-driver. In this way it will prove possible to give more regular and efficient service to customers and to draw up a more stable schedule of rates and charges.

**The Road Clearing House.** We have seen that the road-haulage industry is mainly in the hands of a very large number of small operators, whose facilities for obtaining traffic are necessarily very limited. There exists a definite gap between those who have road transport facilities available for hire and those having goods awaiting transport. This gap is filled by the institution of the *Road Clearing House*, the purpose of which is to act as a link between the trader who wishes his goods carried and the haulier who carries the goods, and in particular to save the haulier the time and trouble of canvassing for return loads. The aim of the road haulier should be to attain the maximum loaded mileage for his vehicles, since his lorries are earning revenue only when they are under load. If he is compelled to make frequent return journeys without a full load, or without any load at all, his rates must be increased accordingly, and this may result in a loss of traffic if his competitors have better facilities for the collection of return loads.

A clearing house has been defined as embracing "all companies, firms, and persons contracting with a trader for the cartage of freight by road motor haulage and sub-contracting for a minimum of 75 per cent of its road freight turnover per annum with a third party for the actual cartage thereof." The first genuine clearing



house was founded in Birmingham by the Ministry of Munitions in 1916, when the limited facilities available for transport made the full utilisation of vehicles an urgent necessity. The success of this clearing house was followed by the establishment of similar institutions under the control of chambers of commerce throughout the country, thereby providing a network of clearing houses at such centres as Manchester, Leeds, Huddersfield, and Halifax. When these were closed down at the end of the War, they were followed in many cases by the foundation of clearing houses under private control, though many chambers of commerce still continue their efforts in this direction.

Unfortunately, although there are many clearing houses in existence rendering valuable service to road haulier and trading public alike, the industry has suffered from the activities of a number of irresponsible institutions whose sole concern is to earn the highest possible rate of commission for themselves. It very frequently happens that so-called "traffic experts" set themselves up in the clearing house business owning no vehicles at all, and obtain their trade by under-quoting the organised hauliers and railways, and then beating down the owner-driver to the cut rate less the clearing house commission. The activities of such concerns are said to be diminishing, but they are likely to remain in existence so long as the road haulage industry retains its present loose organisation. It can be eliminated only by the better education of the small owner and the better liaison among vehicle owners and reputable clearing houses.

In addition to maintaining contact between haulier and trader, the road clearing house renders valuable service in other directions. In the first place, the burden of collecting accounts falls upon the clearing house, so that if bad debts are made, the haulage contractor does not suffer. In addition, the keeping of his own account is greatly simplified. The clearing houses usually settle their accounts with hauliers on a monthly basis, but if a haulier is pressed for cash before the monthly settlement most clearing houses will make him a payment on account. Again, many clearing houses have special arrangements whereby contractors are relieved of the necessity for making immediate cash payments for the supply of petrol and oil or the payment of garage fees. In some cases the clearing houses actually own their own garages and supply the petrol on credit, or



they have an arrangement with a garage in their town whereby they issue orders to drivers, who can obtain supplies without payment on presenting them. In a certain measure, the value of some of these services, from the standpoint of the industry as a whole, is questionable. They tend to keep the small owner-driver of an improvident type in business, whereas it might be to the benefit of the industry if he were eliminated.

### TEST PAPER LVI

1. Account for the revolution in road transport which has taken place during the last quarter of a century.

2. Consider the special advantages of motor transport over competing forms under the headings—

(a) Flexibility, (b) Risk of damage, (c) Cost of service, (d) Speed of transit.

3. Explain clearly, by means of the diagram on page 695, the main types of motor transport engaged in the conveyance of passengers and merchandise.

4. Explain the functions of the Road Clearing House? What services does it render to the haulage contractor and to the community?

5. "The Road and Rail Traffic Act, 1933, constituted an admission that the competition between road carriers and railways in Great Britain was on an unequitable basis but a refusal to adopt an equitable basis." Support or rebut this statement.

6. "In a great city the solution of the passenger traffic problem can only be found by the co-operation of many forms of transport, and each of these has its own merits and requirements." Examine this statement and indicate the traffic conditions best suited to the various forms of urban transport.

7. Discuss the advantages to a large business house of having its own fleet of motor vehicles instead of making delivery by rail or by a road haulage contractor.

8. Write a short account of the existing organisation of the road haulage industry, commenting upon any weaknesses which you see in it.

9. Outline the licensing provisions of the Road and Rail Traffic Act, 1933. To what extent do you consider it likely that these provisions will effect a rationalisation of the road haulage industry comparable with that which has occurred in road passenger transport.

10. "Railway rates are based on the principle of what the traffic will bear, whilst rates for road transport are based on cost."

Explain this statement and discuss the reason for the difference.

11. In what ways would traders and the travelling public benefit from the co-ordination of road and rail transport.

12. "The conveyance of perishable goods illustrates in a marked degree the special advantages that appertain to mechanical road transport."

Comment on this quotation and illustrate your answer by reference to the marketing of agricultural produce.



## CHAPTER LVII

### RAILWAY TRANSPORT

**DEVELOPMENT OF THE RAILWAY.**—The railway was the pioneer of modern mechanical transport, and was responsible for the greatest revolution in communications and the transport of goods that has ever taken place in the history of the world. Indeed, it may be said that up to the time of the Great War, so far as land transport was concerned, the railway held an almost unbroken monopoly. Since the War, it is true, this monopoly has come under strong challenge in consequence of the development of motor road transport, which has created many disturbing problems in this and in other countries. Yet, despite this competition from a rival mode of transport, the railway still retains its essential importance in the economic life of every country, and road transport can never hope to supersede it. The development of great Continental areas—Africa, Australia, or the U.S.A.—has depended upon the construction of a railway, and the economic life of vast regions within those areas is pre-conditioned by its existence. Thus the great wheat industry of Canada was created by the railway and could not continue in existence on its present scale without it. In India the railway has enabled the Government to cope with the disaster of famine in districts which, before the advent of railways, were too distant from the centres of distribution to be helped effectively; they have stimulated economic development by enabling the products of the interior to be brought to the coast for export; they are also of considerable strategic value to the authorities.

Even in our own country, where the competition of the road is far more obvious and effective than in many countries, railways hold their place, and, as far as can be seen, are indispensable for many purposes. Both for passengers and goods, railways are a national necessity, not merely because the railway is the cheapest and quickest method of conveying merchandise and passengers over long distances, but also because for the heavier types of commodities it is still the only practicable form of conveyance. The coal trade and most of the other "heavy" industries are for all practical purposes dependent on the railways, since conveyance



of their products by road is impracticable except in small quantities and for short distances. Furthermore, the railway companies have the inestimable advantage of large and unimpeded arteries of communication running right into the centres of our large cities. In short, the public utility of railways is far from exhausted, and no alternative means of transport now in sight seems likely to make the railway useless.

The railways, in common with many other British industries, suffer from the fact that they were pioneers. Early railway promotions were carried out in an atmosphere of ignorance and prejudice which has left a lasting mark on our railway structure. Frequently land had to be purchased at exorbitant prices from land owners who wished to compensate themselves for the injury which they imagined their property would suffer. The opposition of town corporations often resulted in long and expensive deviations of track. Vested interests, such as the canal companies, opposed the promotion of railway bills in Parliament with the object of getting "bought out" of a business which they could see was doomed once the railway was established. All these things inflated capital expenditure, with the result that the capital costs per track mile are £56,000 in the United Kingdom, as compared with £30,000 for France, and £16,000 for the U.S.A. Moreover, the interest charges on track construction costs alone are calculated by the railways themselves to be not less than £36,000,000 a year. To make matters worse, Parliament, in fear of a railway monopoly of inland transport, deliberately fostered competition by authorising a large number of small separate undertakings. All these things have created difficulties which have persisted to the present day, and are responsible in no small measure for the economic troubles of the railways at the present day.

**STATUTORY CONTROL OF THE RAILWAYS.**—From their inception, the railways have been subject to an increasing degree of Government control designed to protect the public against danger to life and limb and against undue exploitation in the charges. The extent of this interference may be gathered from the fact that during the past hundred years there have been about 200 public Acts dealing with the number and regulation of railways. During the experimental stage of their development, there was relatively little Parliamentary interference, but as their importance became



realised, regulating Acts became increasingly frequent. State regulation in Great Britain has fallen under the following main headings—

- (1) The construction and equipment of the railways.
- (2) Safety of passengers and of employees.
- (3) Securing that reasonable facilities shall be given and that there shall be no undue preference.
- (4) Regulations as to rates, fares, and other charges.
- (5) The rendering of financial and statistical returns.

The motives underlying this mass of regulation have naturally been of a varied character, but the following considerations have exerted a great deal of influence—

(1) **Nature of Railway Construction.** Railways fall within that group of undertakings which is commonly described as providing public utility services, and for the accomplishment of their objects require special powers. Thus, in order to complete a track, compulsory powers may have to be taken for the purchase of land, highways have to be bridged, and other rights of property interfered with. For this purpose, special authority is required from the State, and this authority cannot be given without a preliminary investigation to ascertain whether it is warranted. On this account, British railways are Parliamentary companies, deriving their authority from a special Act of Parliament, and not being incorporated in the usual way under the Companies Act, 1929. Further, the companies are bound by any special legislation governing construction, such as the Railway Gauge Act, 1846, which specifies the standard gauge of 4 ft. 8½ in.

(2) **Special Safety Regulations.** The subject of safety on railways is admittedly very important, and the law provides for elaborate precautions to be taken. It is of public interest that the large number of persons using the railways shall do so with a minimum of risk. Thus the law requires every railway company to give notice to the Ministry of Transport of its intention to open any new section of line for passenger traffic, and place upon that department the duty of inspecting the line before it is opened. Again, railway companies are required to report to the Minister all accidents which have caused, or might have caused, loss of life or personal injury. The safety of railway employees as distinct from passengers, is also



a subject which has been dealt with at length by legislation, whilst the Minister is empowered to make rules for the purpose of removing or reducing the dangers incidental to railway service.

(3) **Danger of Discrimination.** A further motive for regulation was created by a fear of abuse of monopoly which the railways held in the nineteenth century. It was felt that they might abuse their position by withholding reasonable facilities for traffic or by discriminating between different members of the trading public. Accordingly, under the terms of the Railway and Canal Traffic Act, 1854, the companies were bound to "afford all reasonable facilities for the receiving and delivering of traffic upon and from the several railways and canals belonging to, or worked by, such companies respectively, and for the return of carriages, trucks, boats, and other vehicles, and no such company shall make or give any undue or unreasonable preference to, or in favour of, any description of traffic, in any respect whatsoever, nor shall any such company subject any particular person or company, or any particular description of traffic, to any undue or unreasonable prejudice or disadvantage in any respect whatsoever." No definition of "undue preference" has been formulated by Parliament, and the Railway and Canal Commissioners, with whom lies the jurisdiction to determine complaints under these provisions, are more or less free to attach such meaning to the term as appears to them to be proper in a particular case.

(4) **Danger of Excessive Charges.** The nineteenth century railway monopoly created a further fear lest the railways should levy excessive charges. Hence Parliament exercised a continual influence over the rates which the companies were authorised to charge, the general policy being to prescribe maximum charges which could not legally be exceeded, and thus to prevent railway rates from becoming excessive. The charging powers of the various railways were revised under the Railway and Canal Traffic Act, 1888, when uniformity in regard to all the railways was introduced. Under the same Act provisions were inserted whereby the charges for carriage varied according to whether the company provided the wagon or the trader; in the latter case a rebate was allowed from the charge. These charges covered various kinds of services, including collection and delivery, terminal charges and conveyance charges. Charge for detention or demurrage of vehicles was also another authorised charge.



**THE RAILWAYS ACT, 1921.**—When war broke out in 1914 the Government took over the railways and kept them under its control until 1921, guaranteeing to them the net revenue they had had in 1913. But after the War it was obvious that the position required special treatment, and the railways were, in effect, reconstructed under the Railways Act, 1921. The opportunity was taken to re-adjust the relations of the railways to the State, to their employees and customers, and to each other. It was hoped by the Government that the measure would enable the railway companies to bring about economies long desired by the directors and management, that it would assure to the users reasonable facilities at reasonable rates, and would by the provision of adequate and effective cost and operating statistics, enable the proprietors to familiarise themselves with the management of their property. The main provisions of the Act may be classified under the following heads, namely—

(1) **Grouping.** The first part of the Act provided for the grouping into four groups of about 120 separate railway companies; that is to say, practically every railway company of importance in Great Britain. Broadly speaking, each group had a monopoly in its own area, but there was competition where the areas touched or where they overlapped. This step, it was claimed, nearly carried to its logical conclusion the practice of railways in the past, the object being operating economy and administrative efficiency. It was expected that very considerable economies of operation would result, though estimates of their amount varied widely.

(2) **Compensation.** One of the earliest sections of the Act dealt with the settlement of claims in respect of the Government possession of the railways during the War. This was effected by the payment of a sum of £60,000,000 as a full discharge of all claims except those arising out of certain agreements previously made by the Government with the companies.

(3) **Charging Powers.** The Act completely abolished the system of regulating charges previously enforced, and in the place of it substituted an entirely new method. A court known as the Railway Rates Tribunal was set up with very extensive powers, covering every aspect of railway charges. This body was empowered to fix rates, fares, and other charges so that a standard revenue would be earned by each of the groups. The method of arriving at this revenue was carefully defined, and provision was made for its annual



revision, but no guarantee was given that this revenue would be realised. In fact, the new system came into operation at the beginning of 1928, but since that date not one of the four amalgamated companies has realised its standard revenue.

(4) **Relations to Employees.** In order to improve the relations between the companies and their employees, the Act contained elaborate provisions relating to the wages and conditions of service, and provided for a system of conciliation councils with functions not dissimilar to those of the Whitley Councils established in other industries after the War. These bodies are consultative only, and their decisions are not usually enforceable.

(5) **Accounts and Statistics.** Accounts must be prepared on lines indicated by the Minister of Transport, whilst certain statistics and returns must also be made.

Unfortunately the introduction of the Railways Act, 1921, coincided with the commencement of a depression which has gone on ever since. It was particularly bad from 1930 onwards and railways have naturally suffered, though things are becoming slightly better now. Another serious matter for the railways was the growth in the popularity of road traffic after the War. People nowadays have their own cars and their own vans so that the railways lose a considerable amount of traffic in passengers and goods. To some extent also there is the competition of road transport companies.

**THE RAILWAYS IN THE SERVICE OF THE TRADER.**—One of the accusations most frequently levelled against the British railway system has been that of undue conservatism—a failure to make adequate provision for the needs of the trading community. So long as the railways had a virtual monopoly of inland transport, the spur of competition was lacking as a stimulus to greater efficiency. In recent years, however, there are ample signs of a new spirit of enterprise. Thus, the London Midland and Scottish Company has set up a special Sales Department—an entirely new departure in railway work—devoting its whole time to the study of sales methods in industry generally and of how they can be applied to the railways. Again, the London and North Eastern Railway Company has developed a system of travelling motor representatives in order to obtain better liaison and contact with customers with whom contact was difficult previously. Each representative resides in his own



division, where he is available at any time to assist the interests of the company and to help to remove misunderstandings or prejudices regarding railway transport. The following are some of the special services which the railways perform for the trader—

(1) **Warehousing Goods.** This function is of considerable importance to the trading community, and the railway companies are the largest warehousing concerns in the country. The change in trading habits which has taken place in the last few years has greatly increased the demands made upon the railways for storage. The retailer of to-day carries on his business with a minimum of stock relying on speedy modern transport service to make up his stocks. Hence it has become of greater importance to manufacturers that they should be able to execute orders with a minimum of delay, and there has arisen throughout the country a demand for warehouse space for the setting up of branch depots easy of access to customers in the surrounding district. Considerable expense has been incurred in order to adapt these facilities to the needs of trade. Thus at Soho, near Birmingham, in a district which deals largely with non-ferrous metals, a warehouse has been erected for their storage. It is a peculiarity of these metals that their qualities are judged best by daylight, and the warehouse has been fitted with skylights which give the maximum of natural light, while daylight lamps have been provided for inspection when natural light fails. The provision of apparatus for stacking reels of paper, of refrigerators for perishable goods, and of wireless aerials for the testing of wireless sets in warehouses are examples of the steps which have been taken by the railways to meet the needs of those who use their warehouses.

(2) **Registered Transit.** A system of registered transit of merchandise and live stock by goods train, known as the Green Arrow System, has been introduced by the railway companies. Besides providing the quickest possible service for goods it enables the sender to know at the time of dispatch the date and time at which the consignment will be delivered. The arrangement is not confined to traffic passing over a single railway system, but applies also where the consignment passes from one railway to another. It is similar to the registered post, for immediately a consignment is registered it is brought within a specialised control system. The goods bear a distinctive "Green Arrow" label, which ensures prompt handling. The registration fee is half-a-crown for each consignment, which may



consist of a single package or a train-load. This guaranteed delivery system has worked well, for traders in many cases willingly bear the additional cost to ensure delivery by a specified time, as in the case of export by a specified steamer.

(3) **Freight Train Service.** As already indicated, the disinclination on the part of the trading public to tie up capital in large stock has led to a demand for greater railway facilities and quicker journeys in transport generally. The speed of freight transport has been substantially increased of recent years by the acceleration of goods trains. Moreover, goods depots are now much better equipped than they were a few years ago, while improved marshalling yards and better transshipment arrangements have greatly reduced delays in transit, especially on cross-country journeys. Collection and deliveries are better, and for fast freight traffic there are few important industrial centres between which the companies cannot now guarantee delivery on the day following the receipt of the consignment. Another development has been the issue of freight time-tables, which indicate the latest time for the acceptance of goods and the time at which delivery may be expected.

(4) **Container Transport.** Another method of reducing both the time and cost of transportation which has been introduced with considerable success by the railway companies, is the device of the container. This, in effect, is the demountable body of a railway truck or road motor, which being a separate unit from the chassis, has the advantage that it can travel both by rail and road. Goods can be loaded in containers by the sender's experts on his own premises, a minimum of packing being used. In some cases packing can be dispensed with, thereby resulting in an economy of time and material, as well as a saving of freight charges. Containers are available for the conveyance of all descriptions of merchandise, at special tariffs, but the weight of the container is not charged for in either direction. Again, the advantages for international traffic are obvious; not only can goods be consigned direct to a customer, thus avoiding difficult and expensive transshipments, but, given adequate organization, customs control could be simplified by sealing the container at any point, thus ensuring that no change is made in the contents en route. Furthermore, since the containers are constructed in units smaller than railway vans, they can be used with success by customers who cannot take whole van loads. All these advantages



are especially important in the long-distance shipment of perishables, many categories of which cannot stand handling or disturbance en route. Among the traffics for which the container has already become popular are furniture, confectionery, flowers, biscuits, electrical machinery, and meat.

(5) **Rail-head Deliveries.** Another valuable service has been the institution of rail-head delivery by which manufacturers or wholesale firms have been accommodated with warehousing facilities at convenient rail-head depots, and from these depots delivery is made to retailers in the district by lorries, either belonging to the particular firm or supplied by the railway companies themselves. Under this system, goods can be sent in the most economical manner in full truckloads by express freight trains from factories or ports of importation, to be warehoused at the rail-head. Distributors are thus provided with a rail base from which dispatches for a particular area can be made. Amongst the advantages claimed for the system is that of speedy delivery, since retailers are enabled to receive consignments on the day after dispatch. By virtue of this short-period transit, these retailers are relieved of having to maintain large stocks of goods. Again, bulk loading and rail-head delivery mean less handling and the elimination of disturbance to fragile packages. The service does not end here, however, for in the case of a firm whose traffic is sufficient for the full occupation of a road van, the vehicle may bear the firm's own name and style. Firms which deal with numerous commodities obtained from different sources are offered special facilities for assembling their consignments at the rail-head. The railway will allot warehouse accommodation on a moderate rental basis, and will provide clerical services if required. Railway employees are prepared to perform a variety of services in this connection, such as the preparation and regular rendering of stock returns, labelling of goods, and the extraction of samples.

(6) **Miscellaneous Services.** In addition to the foregoing, the railways have, in recent years, shown themselves willing to undertake a variety of services on behalf of the business community. Thus, there have been great developments in the handling of exceptional loads, and there is now much more co-operation between the companies and the manufacturers of heavy machinery. Manufacturers can now obtain full particulars and diagrams of the heavy freight vehicles which the company have constructed for the transport of



loads of unusual size and weight. Another service recently provided by the London Midland and Scottish Railway is the provision of mobile warehouses. These are intended for manufacturers and traders who are engaged upon intensive short sales campaigns in particular areas and desire to hold stocks in those areas from which they can draw supplies at short notice. For this purpose parcels vans with storage capacity of approximately 25 sq.-yd. have been converted into mobile warehouses suitable for the storage of commodities of all kinds. It was stated a short time after this service had been inaugurated that a number of firms had decided to occupy permanent warehouses, since the trade developed in this way justified the expenditure. Again, in 1933 the Great Western Railway Company provided a special train to act as a show room during a three months' tour of the country. This train, fitted up by a private firm to exhibit their goods, was accommodated at stations or in goods yards, where it was open to inspection by the firm's customers.

**RAILWAY RATES.**—The Railways Act, 1921, provided, among other things, for an amalgamation and absorption scheme, with a view to efficient and economical working. The railways were grouped in one of the four groups: Great Western; Southern; London Midland and Scottish; and the London and North Eastern.

The Act also provided for the setting up of a new tribunal called the "Railway Rates Tribunal." To this committee almost all the powers of the Railway and Canal Commission Act, 1888, and many new powers were entrusted, its most important function being the settlement of the schedules and charges of the amalgamated companies. The tribunal consists of three permanent members—one person of legal experience, who is chairman; one person of railway experience, and one of commercial experience. There are also two panels of additional members—one panel consisting of twenty-two persons representing trading interests, twelve representing labour and railway passengers, and two representing agriculture; the other panel consisting of twelve representatives of railway interests. Provision was made for the re-classification and rating of merchandise and the various companies were required to submit a schedule of proposed rates for the consideration of the Rates Tribunal, who, after careful examination, were to fix the charges and to appoint a date for them to come into operation.

**SCHEDULES OF RATES AND CHARGES.**—The duty of determining



## RAILWAY CLASSIFICATION OF GOODS

	Class		Class
Wood, pieces of, japanned (used in the manufacture of Bamboo Furniture), in cases . . .	18	Wooden Boxes (see Boxes).	
Wood, prepared for box-making in bundles or cases . . .	13	Woodware domestic, e.o.h.p., made in one piece and of common wood, not polished nor varnished . . .	16
Wood, prepared for Door Framing or casing-beaded or Moulded (as Mouldings and Beadings)		Wood Wool—	
Wood, prepared for Door Framing or Casing—Rebated not beaded or moulded—(as Planed Boards, see Timber).		Minimum 2½ tons per truck . . .	10
Wood Sash (as Spouting and Sash Wood).		Minimum 2 tons per truck . . .	12
Wood Blocks (see Blocks).		Minimum 30 cwts. per truck . . .	16
Wood Fibre—		Less than 30 cwts. per truck . . .	18
Minimum 2½ tons per truck . . .	10	For surgical purposes . . .	18
Minimum 2 tons per truck . . .	12	Woodwork Carved . . .	20
Minimum 30 cwts. per truck . . .	16	Woodwork for piano making, not polished nor varnished, common wood—	
Less than 30 cwts. per truck . . .	18	Not Veneered . . .	16
Wood Flour (see Flour)		Veneered . . .	18
Wood Frames or Garden Pit Lights (as Frames, Garden).		Woodwork, Organ, e.o.h.p. (see Organ Parts).	
Wood Paling, cleft, wired, in bundles . . .	10	Woodwork, Unstained and unpolished (for the manufacture of Billiard Tables), in parts, in cases . . .	19
Wood Plait (see Plait).		Wool, raw . . .	16
Wood Preservatives (non-dangerous), prepared from Coal Tar. In casks or iron drums . . . (See Exceptional Rate List G).		Wool, dressed or carded . . .	18
In tins in cases . . .	11	Wool Dust (bleached or dyed) used in printing patterns textile fabrics . . .	18
In cans . . .	13	If not in packages declared to be damp-proof as damageable goods not properly protected by packing.	
Wood Pulp . . .	8	Wool Fibre (see Fibre Wool).	
Wood Pulp Boards (as Cardboard).		Wool Hatters' . . .	18
Wood Pulp Fabric (as Textiles)		Wool Nips or Burrs . . .	13
Wood Pulp Yarn (as Yarn e.o.h.p.)		Wool Slag (see Cotton Silicate).	
Wood Shafts for Vehicles (see Shafts).		Wool Tops (as Wool raw).	
Wood Shavings—		Woollen Cloth (as Textiles) (See Exceptional Rate List C).	
In press-packed bales . . .	16	Woollen and Cotton Slops, not oily (as clothing) (Exceptional Rate List D applies to Cotton and Woollen Slops, not oily, in cases, hampers, bales, crates, or parcels).	
E.o.h.p. . . .	18	Woollen and Worsted Goods (as Textiles or Clothing). (See Exceptional Rate List C).	
Wood Sides and Ends for Wire Mattresses not bolted together	13	Woollen and Worsted Yarn (as Yarn).	
Wood Splints for Drapery . . .	13	Wrapping for protecting pipes (see Canvas and Hair Wrappings).	
Wood Splints for Matches . . .	13	Wrappers.	
Packed . . .	16	Newspaper Stamped . . .	20
In bundles . . .	18	Paper unstamped (as Stationery, e.o.h.p.).	
Wood Stain, Powder, solid or solution in water (as Dyes)		Wrappers or Tares, from Cotton Bales . . .	13
Wood Stakes, pointed (see Stakes).			
Wood Sulphite Liquor, Waste (see Lignorsine).			
Wood Supports (not casings) for Electric Cables . . .	13		
Wood Tar (see Tar)			
Wood Tar Oil (as Oils, e.o.h.p.).			
Wood Treads (see Treads).			
Wood Turnings, for fish curing (see Turnings).			



the Rates and Charges to be made for the conveyance of goods in the various classes was undertaken by the Railway Rates Tribunal, which endeavoured to fix the amounts at such a level as would yield each group railway a total annual net revenue equivalent, with adjustment in respect of new capital, to the aggregate net revenues of its component railways in 1913. The task of settling this standard revenue was one of great delicacy, but was completed in July, 1927, when the new rates were sanctioned by the Tribunal and became operative on 1st Jan., 1928. Standardized Schedules of charges for each of the four railway companies were drawn up for—

(1) Goods and minerals, except coal, coke, and patent fuel by merchandise train.

(2) Coal, coke, and patent fuel by merchandise train in owner's wagons.

(3) Returned empties by merchandise train.

(4) Rolling stock by merchandise train.

(5) Animals by merchandise train.

(6) Perishable merchandise by passenger train.

(7) Small parcels by merchandise train.

(8) Passengers.

The railways retain the power, under carefully guarded conditions, of making new exceptional rates—a provision which gives them some degree of the elasticity essential if they are to conduct their business on commercial lines.

**GOODS AND MINERALS.**—This is the most important group, since it includes the bulk of commodities consigned and received by British traders. It is subdivided into twenty-one classes. No. 1 is the lowest class, and applies to the roughest and cheapest goods ; whilst No. 21 applies to the most valuable.

Examples of the commodities included under these different classes are as follows—

- |       |  |
|-------|--|
| Class | 1. Cinders and ashes for road repairs, iron ore, limestones in bulk. |
| „     | 2. Sand in bulk, bricks, gravel stone (undressed).                   |
| „     | 3. Ammoniacal liquor, lime (in bulk).                                |
| „     | 4. Salt rock, creosote.  |
| „     | 5. Pig iron, common clay, manure.                                    |
| „     | 6. Ground slate, coal tar pitch, china clay.                         |
| „     | 7. Pit props, iron and steel plates, plaster.                        |
| „     | 8. Wood pulp, wire, petroleum pitch, and grain.                      |
| „     | 9. Marble, Fuller's earth.   |
| „     | 10. Hay and straw, tin, nickel, and sawdust.                         |
| „     | 11. Granite, sheet lead, tallow, and sugar.                          |



# LONDON MIDLAND AND SCOTTISH RAILWAY

Scale of Charges in respect of Goods and Minerals, except Coal, Coke, and Patent Fuel, by Merchandise Train  
Applicable to traffic elsewhere than in Scotland

Class in respect of Merchandise to which charges are applicable	STANDARD RATES FOR CONVEYANCE				Station terminal at each end	STANDARD TERMINALS			
	For the first 20 miles or any part of such distance	For the next 30 miles or any part of such distance	For the next 50 miles or any part of such distance	For the remainder of the distance		SERVICE TERMINALS			
	Per Ton per mile d.	Per Ton per mile d.	Per Ton per mile d.	Per Ton per mile d.		Loading	Unloading	Covering	Uncovering
1 } 2 } 3 } 4 }	1-90	0-95	0-55	0-50	Per Ton s. d. 3	Per Ton s. d. —	Per Ton s. d. —	Per Ton d. —	Per Ton d. —
	2-15	1-05	0-70	0-65	5	—	—	—	—
	2-25	1-10	0-80	0-70	6	—	—	—	—
	2-30	1-20	0-90	0-75	10	—	—	—	—
5 } 6 } 7 } 8 }	2-60	1-25	0-95	0-75	6	—	—	—	—
	2-65	1-35	1-05	0-80	10	—	—	—	—
	3-05	1-80	1-35	0-95	1	5	5	1-25	1-25
	3-20	1-90	1-45	1-00	1	5	5	1-25	1-25
9 } 10 } 11 } 12 }	3-40	2-10	1-70	1-15	1	5	5	1-50	1-50
	3-50	2-30	1-85	1-25	1	7	5	1-50	1-50
	3-65	2-55	2-10	1-45	2	—	6	2-50	2-50
	3-75	2-65	2-20	1-60	2	—	8	2-50	2-50
13 } 14 } 15 } 16 }	4-05	2-85	2-40	1-75	2	5	8	2-50	2-50
	4-40	3-15	2-75	2-15	2	5	10	3-00	3-00
	4-75	3-45	3-00	2-25	2	5	11	3-00	3-00
	4-80	3-55	3-10	2-35	2	5	1	3-00	3-00
17 } 18 } 19 } 20 }	5-35	4-10	3-35	2-55	2	5	1	3-00	3-00
	5-50	4-25	3-50	2-75	2	5	1	3-00	3-00
	6-40	5-15	4-25	3-50	2	5	2	5-00	5-00
	7-50	6-20	5-10	4-30	2	5	2	6-00	6-00
21 }	11-25	9-30	7-65	6-45	3	7	4	9-00	9-00

Fractions of less than one halfpenny in the rate to be dropped, and fractions of one halfpenny or over to be charged as one penny.



- Class 12. Brass, machinery.  
„ 13. Mustard seeds, raw cotton, oils.  
„ 14. Lead, brass tubes.  
„ 15. Lard and lard substitutes, sage, cotton yarns.  
„ 16. Fish, paper serviettes, bulbs.  
„ 17. India-rubber, tomatoes in baskets with paper covers.  
„ 18. Boot laces, dry yeast, tea, silver.  
„ 19. Dead rabbits, razor strops, cotton lace, wine in hampers.  
„ 20. Perfumery, live rabbits, pianos and scientific instruments.  
„ 21. Liquid gold, gold articles.

A complete list of these goods is given in the *General Railway Classification of Goods by Merchandise Trains*, an extract from which is given on page 713.

The standard rates for conveyance as well as the standard terminals are now uniform throughout the whole country, and are common to all the railways. From the scale of charges shown in the table on page 715 it will be seen that there are two main factors to be considered—the type of traffic and the distance. As regards the nature of the goods those that are costly, or easily damaged or lost, are charged at a higher rate to compensate for the extra risk and for the extra care that must be expended upon them. Further, as between goods of higher and lower values, the rule applied is “to charge what the traffic will bear.” This means that a fairly high rate charged for the carriage of valuable goods causes little proportionate increase in their cost to the consumer, whereas the same rate applied to goods of low value would render the price prohibitive. As regards the distance, it will be seen that a “tapering” rate has been adopted. Thus a certain charge is made for the first twenty miles, a reduced charge for the next thirty miles, a further reduced charge for the next fifty miles, and a still further reduction for the remainder of the distance, so that the charge per mile decreases as the distance increases.

Except otherwise provided for in the classification, the minimum weights which can be conveyed at the standard rates are 6 tons for classes 1 to 6 ; 4 tons for classes 7 to 9 ; 2 tons for classes 10 to 11 ; for the remaining classes there is no minimum. Where less than the stipulated minimum is consigned goods are charged at a higher rate.

**STATION TERMINALS.**—From the table on page 715, it will be seen that the maximum is fixed for a station terminal, and is chargeable at each end of the journey. This charge is mainly for the rent of the station ; the siding accommodation ; the warehouse



accommodation, where the goods are loaded and unloaded. It also covers the shunting work, the placing of wagons into position in loading and unloading.

The charge varies from 3d. per ton to a maximum of 3s. 7d. At first sight, this 3d. looks extraordinarily low; but it must be borne in mind that it applies to a class of traffic which it is expressly stated must be consigned in minimum lots of 4 tons, or a higher rate will be charged.

**SERVICE TERMINALS.**—This group includes loading and unloading, covering and uncovering; and the two last mentioned include not only the work involved, but also the use of the sheet.

It will be noticed that there are no service terminals entered against Classes 1 — 6. The reason for this is that the railway is under no obligation to do the work of loading and unloading for these traffics. Should they consent to perform these services, a reasonable charge may be made, in addition to the tonnage rates. The slightest fractional variation in the charges made for terminal services means a considerable change in the revenue of the company, owing to the enormous amount of traffic carried. This is of importance when considering what rates ought to be charged, and it shows the necessity for accurate statistics being kept.

**Other Services which the Railways may charge for,** and for which they are restricted to a reasonable sum, are—

(1) *The services rendered by the railway company at, or in connection with, the private sidings.* If the railways are to be allowed to charge undefined charges for services rendered at a private siding, that implies that other charges shall not be made. No trader can claim to do the work in connection with his goods if his consignment is mixed with other goods in the wagon. Otherwise, the trader can claim the right to do the terminal services, carry them out with his own servants, and in that case the company may not charge for them.

(2) *The collection and delivery of merchandise outside the terminal station* (i.e. the cartage). It is the usual practice of most railways to include in the ordinary class rates the services of collection and delivery at all places where they undertake such work, so that in all the ordinary class rates—where railways do the work—there are certain rates for cartage which are not subject to statutory maxima, except that they “shall be reasonable”;



where the trader is allowed to do the carting himself, he is entitled to a rebate and the removal of the charge for cartage.

(3) *Weighing.* It might be argued that the traffic would (in any case) have to be weighed, but the trader is responsible for the weighing of the traffic which he tenders to the railway company. If the trader requires to know the weight, then the railway authorities are entitled to charge him for the service—otherwise they are not bound to tell him. In the case of small consignments, the railway companies, as a rule, enter all weights and do not require the traders to declare them; but in the case of the coal trade the railways do not weigh the bulk of the coal wagons—the colliery owner is made to declare the weights. The colliery owner has to provide his own weighing machine and supply the weights to the company.

Another instance is that of the conveyance of bricks. The bricks are loaded at some private siding, and very often are never taken near a place where they can be weighed by the railway company. The trader is, therefore, called upon to declare the weight. The railway company sends an inspector round to weigh small quantities of bricks picked out at random, and thus argues that a larger quantity will weigh in the same ratio.

(4) *The detention of trucks* beyond a reasonable period by the trader is subject to a *demurrage charge* imposed by the railway company; and a trader can also be charged if he loads up his goods and then neglects to give a consignment note stating their destination.

(5) *Provision of accommodation at a waterside wharf* and any services rendered thereat.

In some cases, in the collection and delivery of goods, there are services which the railway companies need not render at all unless they choose. The great bulk of the railway companies of the world do not render the services of collection and delivery. They confine themselves to station and station, and the cartage work is left as an outside industry to be carried on by firms of local carriers. Hence, among this list of services there are two distinct and different kinds—

(1) A batch that the railway companies *must* at times render, and which they are under legal obligation to render.

(2) Another batch where they are under no legal obligation



at all to render, since it is a purely voluntary act; and if the railway company renders these services, it must not charge more than a "reasonable sum."

**Calculation of a Rate.** The procedure for the calculation of any commodity coming within any one of the twenty-one classes above mentioned is as follows—

I. Refer to the "General Classification" in order to find out the class to which the particular commodity belongs.

II. Ascertain from a railway guide the distance the goods are to be transported.

III. Calculate the rate for conveyance according to the particular class from the Table on page 715.

IV. Add to the No. III the station and service terminals, together with the charge made for cartage.

An example will make this clear. Suppose a consignment of raw wool, weighing 10 cwts., is to be sent from London by the London, Midland and Scottish Railway a distance of 112 miles. The rate would be calculated as shown below.

RAW WOOL = *Class 16 commodity—*

	<i>d.</i>	<i>d.</i>
∴ First	20 miles @ 4.80 per mile =	96
Next	30 „ „ 3.55 „ =	106.5
„	50 „ „ 3.10 „ =	155
Remainder	12 „ „ 2.35 „ =	27
	<hr/> 112 miles	<hr/> = 384.5
	<hr/>	<hr/>

Add Station Terminals—

2s. 5d. per ton at each end = 58

„ Service Terminals—

Loading . . . . .	13
Unloading . . . . .	13
Covering . . . . .	3
Uncovering . . . . .	3

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474.5

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Rate for 1 ton (excluding cartage) = 475

∴ 10 cwts. = 237 = 19/9



In case a through rate is required (i.e. the goods pass over the lines of two or more railways), the only difference in the calculation would be—

(a) The amount traversed on each line must be ascertained.

(b) The maximum rates of conveyance for each line are calculated separately and then added together.

Railway companies are compelled to keep rate books at their stations containing the rates to be charged for freight in each of the twenty-one classes into which "Goods and Minerals" are divided. They may not charge any rate to the public which does not appear in those rate books. Any such rate would be illegal, and the railway company is liable to prosecution. Moreover, the rate books must be open to the public for inspection, without fee, at all reasonable hours whilst the station is open. These conditions are the guarantee to the public that the treatment they receive shall be equal. Since the existence of the preferential treatment of one person over another depends upon secrecy, the importance of keeping the rate books open to the public inspection is self-evident.

**OWNER'S RISK.**—Goods may be dispatched at "Company's risk" in which case the company is responsible for their safe delivery; or they may be sent "Owner's risk," in which case the company is freed from all liability except as regards damage caused by the neglect of its servants. In consideration of being relieved of the ordinary risks of the journey the company charges a smaller fee for its services. Every consignment of merchandise forwarded at owner's risk rates must be addressed in accordance with the company's regulations, and must be accompanied by a consignment note on which shall be stated that the consignment is to be carried at "O.R." or "Owner's risk." The traffics to which the scale applies are indicated in the classification of goods by the letter *a*, *b*, *c*, *d*, *e*, *f*, *g*, or *h*. Other traffics are charged at the "C.R." or "Company's risk" Standard Rate in the absence of an exceptional rate.

**RETURNED EMPTIES.**—There is also a special scale of charges for "returned empties."

"Returned empties" here mean that the "empties" are sent from the same station and from the same consignee to which and to whom they were carried, and they must be returned to the



same station and the same consignor from whom they were carried. Thus, in the case of a "returned empty"—

(1) The terminal stations must be the same.

(2) The consignor and the consignee must be the same, except that their positions are reversed.

Empties which are not "returned empties" are charged at much higher rates, and, therefore, the word "returned" makes a considerable difference in the expense involved by the trader.

**CARRIAGES.**—The scale of charges for carriages applies to vehicles which cannot be sent on their own wheels. The statutory scale provides that for the first fifty miles the rate of conveyance is 9·6d. provided the vehicle does not exceed a ton in weight. For the next fifty miles the rate is 5·30d., and for the remainder of the distance 5·10d. The charge for station and service terminals is fixed at so much per ton.

**ANIMALS.**—The scale of charges for animals takes the same form as that for goods and minerals, and there are also station and service terminals. The station terminal at each end is 8d. per head, whilst the service terminals for loading and unloading are 3d. per head. The charge for conveyance is 3·75d. per head per mile for any distance up to twenty miles. Thus the rate of conveyance for a distance of fifteen miles would be  $15 \times 3\cdot75d. = 56\cdot25d.$  As in the case of goods traffic, the rate diminishes with an increase of distance.

**DANGEROUS GOODS.**—There is also a special classification for explosives and other dangerous goods for conveyance by merchandise trains, and only those provided for in this classification will be accepted by the companies. The question whether goods are dangerous is determined by the Railway Rates Tribunal, and such goods are subject to an indemnity which was imposed for the first time by the Railways Act, 1921.

**PERISHABLE GOODS.**—Up to the passing of the Act of 1888 the carriage of goods by passenger train was a purely voluntary act on the part of the railways. The only types of goods they were compelled to carry up to that time were the personal luggage of passengers, mails sent by the Post Office, and Parcels Post. Under the Railway and Canal Traffic Act of 1888 and the Order Confirmation Acts of 1891–92, this position was altered, and for certain classes of traffic it was made an obligation on the railway



companies to carry certain traffic by passenger train. Reasonable facilities were to be afforded for the expeditious conveyance of perishables, although such facilities were to be subject to the convenient and punctual working of the passenger train service. It should be noted, however, that only perishables given in a particular list were to be conveyed compulsorily by the companies. This list of perishables can be divided roughly into four classes—

(1) Dairy and poultry farm produce (e.g. butter, milk, cheese, eggs, etc.).

(2) Fish and ice, which seem to go naturally together.

(3) Fruit and hot-house vegetables.

(4) Game, rabbits, and meat.

**CONVEYANCE OF PARCELS BY PASSENGER TRAIN.**—As has already been mentioned, most of the railway companies convey small parcels by passenger train on payment of a fee in accordance with the authorised rates, provided the parcels do not contain anything of a fragile nature. The parcels must be delivered at the station from which they are to be sent at least ten minutes before the departure of the train by which they are intended to be forwarded. In all important towns, the companies collect free of charge, and also deliver free of charge within the ordinary delivery limits of principal stations.

When speaking of “parcels” by passenger train, the word “parcel” means a package. A package might consist of three or four parcels, provided they are firmly fastened together so as to make one package for purposes of handling.

To this rule there are exceptions—

(1) There may be an exception if, on arrival at destination, the parcel is required to be split up and delivered to different people. In that case, the charge has to be made as for separate parcels.

(2) There is also a statutory list of exceptions.

**SMALL PARCELS BY GOODS TRAIN.**—Any consignment not exceeding 3 cwts. is considered as coming under the heading of small parcels, for which there is a special scale of charges. The term “parcel” is here used to signify a consignment which may consist of several parcels or packages. There is a condition that the railway is entitled to insist on every parcel weighing 14 lbs. and, if it does not, to charge for each parcel as 14 lbs. In practice,



however, little notice is taken of this provision. A minimum of 28 lbs. in weight may be charged for by the railway companies, and this is taken full advantage of by them. Reference to the scale for small parcels in the General Railway Classification Book will show that nothing less than a quarter is quoted.

**RAILWAY CLEARING HOUSE.**—Owing to the fact that it is practically impossible to convey goods or passengers any considerable distance without having to traverse the lines of more than one company, some device had to be introduced to enable the different railway companies to divide between them the through fares or goods rates. This was effected by the institution of the Railway Clearing House in the year 1842, which obtained Parliamentary recognition by the *Railway Clearing Act* of 1850. All traffic which passes over more than two companies' lines is dealt with here. The various companies render to the Clearing House a monthly return of all through bookings, whether passengers, goods, parcels, or any other kind of traffic; and the business of the Clearing House is to deal with these returns in such a manner that each company is credited with its fair share of these bookings. When two companies only are concerned, the division of the receipts is usually a matter of mutual arrangement, and is not dealt with through the Clearing House.

The traffic returns published by the Clearing House are very serviceable in discovering the extent of the country's trade. An increased amount of receipts in the heavy or goods traffic shows an enlarged conveyance of coal, iron, cotton, and so on, which indicates, therefore, a revived condition of those industries; while diminished receipts upon the southern or passenger lines imply a reduction in the extent of the continental and holiday traffic.

**FUTURE DEVELOPMENT OF RAILWAY TRANSPORT.**—A Report presented to the Minister of Transport by the Transport Advisory Council in April, 1939, dealt with the railway companies' claim to what they had epitomised as "a square deal." The Report insisted on the desirability, and even the urgency, of a proper co-ordination of all forms of transport for the sake of both national economy and national efficiency. In the main, the claims of the railway companies for release from unfair and obsolete restrictions are allowed. The Council recommend the repeal of the present provisions relating to the classification of merchandise and the fixing of standard charges.



This relaxation amounts to putting the railways on equal terms in their competition with road transport. At the same time, both industries and individual traders are confirmed in their right of appeal to the Railway Rates Tribunal for a reduction of any charge. It is necessary to ensure that the protection thus given to the individual trader will be sufficient for his needs. There are also to be periodical meetings between the railways and the traders for the discussion of matters of common interest and for the avoidance of friction. Not unnaturally the Report is regarded with much satisfaction by the railway companies, and it only remains for Parliament to give statutory effect to the Council's recommendations.

### TEST PAPER LVII

1. Into how many classes may railway rates be divided ?
2. State the number of classes into which goods and minerals are divided for the purpose of fixing railway rates.
3. Explain the principle which determines the class into which a commodity is entered for the purposes of the "General Railway Classification of Goods by Merchandise Trains."
4. What is meant by the charge for station terminals ?
5. Explain what is included under the heading of service terminals in the Table on page 715.
6. What in your opinion are the reasons for the standard rates of conveyance shown in the table on page 715, decreasing as the distance increases ?
7. Mention any services which railway companies may charge for, but for which they are restricted to a reasonable sum.
8. On what basis does a railway company charge for conveying goods from one town to another ?
9. Why does it cost more to convey a ton of worsted coatings by rail between Bradford and London than a ton of raw wool ?
10. From the scales of standard charges shown on page 715, calculate the following rates—
  - (a) L. to P. 78 miles apart, railway A : Class 10 goods.
  - (b) L. to P., 130 miles, railway B : Class 12 goods.
  - (c) P. to P., 95 miles, of which 60 are by railway B, 35 by railway A, Class 4 goods.
  - (d) P. to P., 54 miles apart [17 railway A, 37 railway B], Class 11 goods.

A = L. M. & S. Railway	L = London
B = S. Railway	P = Provincial Towns
11. What is meant by Class Rates ?
12. Name any classes of goods other than goods and minerals for which there is a special scale of charges for conveyance by rail.
13. Explain the meaning of "returned empties."
14. What is the object of the Railway Clearing House ?
15. Explain the following : "Owner's risk" rates ; perishable goods ; company's risk.
16. Indicate the factors that are taken into account by a railway company when classifying goods offered for conveyance by rail. Has the trader any means of redress if his goods, in his opinion, are wrongly classified ? If so, explain the procedure.



## CHAPTER LVIII

### OCEAN TRANSPORT

**IMPORTANCE OF SHIPPING.**—It would be difficult to exaggerate the importance of the shipping industry in the economic life of this country. As the Balfour Committee pointed out, the fact that the bulk of our external trade is carried by sea, while in addition coastwise steamers perform to a large extent the transport services rendered in some other countries by river and canal, it is clear that ready access to an adequate supply of efficient sea-carrying power on reasonable terms is one of the prime conditions of competitive power. From the time when the iron ship began to drive the wooden ship off the high seas in the middle of the nineteenth century and our merchant marine repelled the challenge of American shipping, British ships dominated the carrying trade of the world up to 1914. In the past decade that supremacy has been challenged by many countries, who have attempted by direct subsidy, by restrictive conditions in coastwise trade, and in other ways, to create for themselves a merchant fleet of their own. Yet, even to-day, over one-half of the tonnage passing through the Suez Canal flies the British flag, whilst British ships carry 90 per cent of inter-Imperial trade, 60 per cent of the trade between the Empire and foreign countries, and 25 per cent of exclusively foreign trade.

The ship is by far the largest vehicle which has ever been devised by man, and its cargo-carrying capacity is greater than that of any other single transport unit. As compared with the motor vehicle or even the railway train, the cargo space available on the modern ship is enormous, whilst developments in shipbuilding technique are constantly increasing the cargo space in relation to the total capacity of the ship. The vessel can be operated with a relatively limited crew, whilst its permanent way is provided freely by Nature. Consequently, goods can be transported more cheaply by this method than by any other, and rates for certain cargoes are as low as  $\frac{1}{10}$ d. per ton mile. Furthermore, the competitive conditions normally prevailing in the shipping industry operate to keep these charges down to a minimum, which benefits the trader in the freight charges which he pays on his goods. At the same time, it may create



difficulties for those engaged in the industry and invite action to restrain the competitive struggle.

One development which has occurred in recent years—the large-scale transfer from coal-using to oil-using vessels—has been of considerable economic significance to this country. Formerly the mining industry of this country supplied a large amount of coal annually for bunkering ships and maintained coaling stations all over the world. The maintenance of stocks at these stations provided outward cargoes for a considerable tonnage of ships, but with the decline in the demand for coal the shipping trade and the coal industry have suffered alike.

**CLASSIFICATION OF SHIPPING.**—The facilities afforded by shipping firms may be classified according to the type of carrying function which they perform, namely, the conveyance of passengers and of merchandise. This classification is not, however, a particularly good one, since there is no clear line of distinction between the vessels engaged in these two types of traffic. It is true, of course, that luxury liners, such as the *Queen Mary*, cater mainly for the requirements of passengers, but at the same time they perform a certain amount of cargo-carrying work in connection with goods of the more expensive types. On the other hand, ships devoted mainly to cargo-carrying work often carry a certain number of passengers as well. Between these two extremes we find ships engaged in both classes of work in varying proportions. We may, however, adopt a classification based on the manner in which a line is organised, and may distinguish the following classes.

(1) **Passenger Liner Services.** The essence of a liner system is the maintenance on a given route of a regular service of ships sailing on advertised dates, whether full or not. The liner under this heading is designed primarily for the carriage of passengers and mails, and is therefore designed for both speed and luxury. The Atlantic trade has provided conditions which have allowed the development of this tendency to the greatest extent. The transatlantic service by steam has now been in existence for well over a hundred years, and for practically the whole of that period the ships on it have been the largest, finest, and fastest in the world. Unfortunately, of recent years trade depression has reduced the number of travellers making use of these ships, and traffic has tended to move from the very luxurious and expensive liners to the slower and cheaper boats.



# OCEAN LINER ROUTES

Route	Area Served	Ports of Departure	Ports of Call	Chief Steamship Lines
I. North Atlantic Route.	This route links the ports of Western Europe with those of the East of North America. Besides Canadian products, cotton and fruit are derived from the eastern States of the U.S.A.	Glasgow, Liverpool, Manchester, Southampton, Dover, and London.	Quebec and Montreal (summer only), Halifax, St. John, Boston, New York, Baltimore, Charleston, Galveston, and New Orleans.	(1) Cunard Steamship Co. (2) White Star Line.
II. Suez Canal Route.	This route commands the markets of Eastern Africa, Persia, Arabia, India, the Far East, and Australia. Besides the special Indian, East African and Australian products, the trade includes Arabian gum, Persian carpets, and opium, East Indian sugar and spices, Manila hemp and tobacco, Chinese tea and silk; and the products of the Mediterranean—fruit, wine, maize, wheat and cotton.	London, Liverpool, and Southampton.	Lisbon, Gibraltar, Algiers, Marseilles, Genoa, Naples, Malta, Port Said, ALEX., and Bombay; Calcutta, Penang, Singapore, Manila, and Hong-Kong; Perth, Adelaide, Melbourne, and Sydney; Mombasa, Zanzibar, Mozambique, Delagoa Bay, and Durban.	(1) Peninsular and Oriental S.N. Co., Ltd. (2) The British India Line, (3) The Australian Commonwealth Line, (4) Japan Mail Steamship Co., Ltd.
III. The Cape Route.	Besides the special South African and West African products, the trade along this route includes the rubber, palm oil, and ivory of the Congo. The route also controls part of the Australian market.	London, Liverpool, Southampton, and the Severn Ports (Bristol, Cardiff, and Swansea).	Maderia, Las Palmas, Tenerife, Ascension, St. Helena, Capetown, Port Elizabeth, and East London; Cape-town, Fremantle, Adelaide, Melbourne, Sydney, and Brisbane.	(1) Union Castle Line. (2) Australian Commonwealth Line. (3) P. & O. Line.
IV. The Plate Route.	This route includes the Brazil trade in rubber, coffee, rosewood, diamonds, and the typical Plate trade in grain, wool, and meat.	Liverpool, Southampton, Glasgow, Manchester, and London.	Lisbon, Madeira, St. Vincent (Cape Verde Is.), Manaus, Pernambuco, Bahia, Rio de Janeiro, Santos, Monte Video, Buenos Aires, Rosario, Punta Arenas.	(1) Royal Mail Steam Packet Co. (2) Pacific Steam Navigation Co. (3) Lamport and Holt Line.
V. The West Indian Route.	Besides the special West Indian products of sugar, bananas, and raw cotton, the trade includes Mexican mahogany, tobacco, and silver.	Bristol, Manchester, Southampton, and Liverpool.	New Orleans, Galveston, Kingston (Jamaica), Havana, Vera Cruz, and Tampico.	(1) Elders & Fyfe. (2) The Imperial Direct West Indian Mail Services Co., Ltd.
VI. The Panama Route.	This route taps the Pacific coasts of America and constitutes a direct route to New Zealand.	Southampton, Liverpool, and London.	Colon, Pacific Coast, and New Zealand Ports.	(1) New Zealand Shipping Co., Ltd. (2) Royal Mail Steam Packet, Co.



(2) **Cargo Liners.** This type of vessel carries larger quantities of merchandise and fewer passengers than the foregoing, whilst her accommodation is not usually of such a luxurious order. These vessels usually operate on routes where speed is not the main requirement, and where cargo as well as passengers make her running a paying proposition. They include many of the fastest and most efficient freighters, and they are generally fitted for the particular traffic on the routes on which they operate. Thus, many of them are equipped with refrigerating machinery and insulated holds for the carriage of meat or of other perishable cargoes. These boats, in common with the passenger liners, operate on a fixed time-table, so that they provide a service which can be relied upon by traders who have to make delivery of goods in a stipulated period.

(3) **Tramps.** The main features of the tramp system are that, unlike the liners, the tramp has no fixed itinerary and sails only if she has a cargo to carry or one in prospect. Fleets of tramp steamers may be compared with fleets of cabs waiting for employment in the streets, and ready to carry out their fares' instructions. Normally, the tramp vessel, like a taxicab on the ranks, is in a position to be chartered at any moment. Her owners try to secure outward and homeward freights, fitting well together to make a complete round venture. The shipper, or shippers, charter a vessel to go where required, but she does not normally take cargo in parcels as the liners do, but deals almost entirely with full cargoes. The seasonal movements of trade give tramp vessels their great opportunities for employment, such as the trade in grain and other commodities harvested at definite seasons. Freight rates are international, the same rate being paid for a ship of equal class sailing under any flag, that is, in the absence of any State regulation.

**THE CONFERENCE SYSTEM.**—The object of a liner company is to maintain a regular service along specified routes, but in order to perform this function the company must be in a position to rely upon the regular support of shippers. As we have already pointed out, the sea is a highway which is free to all persons, and a vessel may sail on it without purchasing a right of way. A railway is tied to its own route, but a ship is free to move where it wishes. Hence it is difficult to restrict the shipments on any given ocean route to a single carrier or combination of carriers. Yet, the position of a liner company may be rendered almost untenable if tramps are able



to cut in at any time when conditions are favourable and take all the most profitable cargo at rates which are much lower than those which the liner company can afford to accept.

A partial restriction of liner competition has been possible because it is a costly venture to establish a line of fast steamers. The number of ocean lines is consequently limited, and if the small number of rivals can come to an agreement as to rates, division of traffic, or pooling of earnings, competition can be regulated and some measure of monopoly can be established. In order to protect the services which they have organised, shipowners in all the great trades have formed themselves into *Shipping Conferences*, which are periodical meetings of the representatives of the various lines concerned in each particular trade to discuss matters which affect that trade and to agree upon uniform rates for the various classes of cargo. Each conference has its own area, and in certain cases where several trade routes intersect or adjoin one another, the various conferences have understandings or agreements with one another to respect each other's spheres of influence.

The principal advantages claimed for the system are that by means of conferences regular sailings and systematic rates of freight are obtained. The greater regularity of sailings is serviceable to merchants, since it is not necessary to engage cargo space a long time in advance, and definite dates can be assigned for the delivery of goods. By the adoption of uniform freight rates, combined with stability, shippers can calculate transport costs with a feeling of security. At the same time, discrimination of rates in favour of the large shipper is eliminated. On the other hand, it has been urged that such conferences led to dictatorial methods on the part of members; that their policy was one of high freights, and that State supervision of their activities was required. More recently they have been criticised from within on the ground that the company which has been enterprising enough to build up the finest fleet has to carry its weaker associates. There is also the difficulty of getting all parties to adhere honourably to the conditions they have themselves laid down.

**DEFERRED REBATE SYSTEM.**—The tie with the shippers of the goods that the conference lines seek to establish is secured in a variety of ways, the chief of which is known as the deferred rebate system. The conferences could not provide the benefits of stability



of rates and regularity of service unless they had some assurances of continuous support from their customers. The fact that a trade was open to all shipowners would lead to the incursion of outside ships at times when the trade was flourishing, but these outside ships would quickly disappear when the seasonal or periodic depression set in, leaving the regular lines to bear the brunt of this depression. The conferences adopt the view that they could not continue in times of bad trade to furnish regular services in which ships often sail with little cargo unless in times of good trade they are permitted to carry all the cargo offering.

The deferred rebate system operates in the following manner. The companies comprising the conference issue a notice to shippers informing them that, if at the end of a certain period, say six months, they have not shipped goods by any vessels other than those dispatched by members of the conference, they will be credited with a sum equivalent to a certain part (usually 10 per cent) of the aggregate freights paid on their shipments during that period. This sum will be paid over to them, however, only if at the end of a further six months they have continued to confine their shipments to vessels belonging to members of the conference. The sum paid in this way is known as a deferred rebate. If a shipper has consigned goods by more than one company in the conference, he claims from each of those companies the amount of rebates due upon his shipments in each case.

The shipowners claim that they are able, by means of the deferred rebate system, to confer the following advantages on their customers.

(1) Greater stability of freight rates is possible. Before the introduction of the rebate system, freights were subject to sudden fluctuations, which led to sudden changes in the values of imported stocks. Under the rebate system, however, rates are stable, except for progressive reductions or increases.

(2) There is equality of rates for all shippers, whether large or small, as regards general merchandise. The only exceptions are full or large cargoes of heavy materials, such as steel rails, which may be the subject of special contracts, since they are suitable for carriage by tramps and may otherwise be taken that way.

(3) Conference lines operating the system supply frequent, regular, and efficient services, and from the point of view of the shipper this is worth some concession.



(4) In the days before the introduction of the rebate system it was customary for shipowners on occasions to buy goods on their own account to fill up their ships, thus competing with the merchants; whereas, under the rebate system, it is tacitly understood that shipowners will not make any shipments on their own account.

Shippers, in general, admit these advantages, but express certain objections to the working of the system. They contend that it enables steamship conferences to maintain a monopoly and to set limitations to the shippers' freedom of action. They point out that the shipowners tie their customers to them, and thus render it difficult for any other shipowner to start a service in their particular trade. The following complaints have also been made—

(1) The periods adopted in connection with the system are too long, and that even when the deferred rebate is due, a delay of months may occur in checking and adjusting the claim.

(2) That the system keeps large amounts of the shippers' capital locked up.

(3) That the system is too complex and entails an undue amount of clerical labour.

Another form of the tie is the *Agreement System*, which takes the form of a contract whereby a trader undertakes during a defined future period to give all his custom to the conference, and in return is charged a lower rate of freight than shippers who have entered into no such agreement. In return, the lines undertake to maintain regular sailings at advertised dates, the ships to sail full or not full, and to provide sufficient tonnage for the ordinary requirements of the trade. Further, they agree to maintain stability of freights, which are definitely prescribed in the agreement, and equality of rates to large and small shippers alike. This system is in force in the South African trade, since deferred rebates are forbidden by South African law. In the Australian and New Zealand trades, traders have the option of using either system on equal terms.

**SHIPPING DOCUMENTS.**—The document constituting the contract of carriage by sea depends upon whether goods are being consigned in relatively small quantities, or by the shipload. In the former case, the contract is contained in a bill of lading, but in the latter, a charter party. The characteristics of these documents are as follows—

**The Charter Party.** When goods are to be forwarded in large



consignments, it may be to the interest of the merchant to hire or charter a ship. The centre of the chartering business is London, and the persons who undertake this kind of work are shipbrokers. The contract which constitutes the basis of the chartering is known as the "Charter Party." This ancient document, which used to be made out in two parts, commences by warranting that the ship is staunch and strong, and goes on to define the conditions of hire, etc. The captain and crew regard the charterer as the interim holder, and they take their instructions from him.

(A specimen Charter Party is shown by inset.)

From the Charter Party, it will be seen that the chief items of agreement are—

- (1) The places between which the ship is to go ;
- (2) The cargo to be carried ;
- (3) The freight to be paid for the work.

There are also some minor items, such as the manner in which the freight is to be paid ; the number of days, called *lay days*, which the shipowner is willing to allow his ship to remain in port for the purpose of loading and unloading ; and the sum to be paid per day for any time she is detained by the charterer over and above the number of days mentioned in the contract. This last payment is known as "demurrage," and should be collected by the master of the ship from the charterer or his agents as it becomes due.

If the payment to the shipowner is to be made at an agreed rate per ton, and the charterer is unable to provide sufficient goods to make up a full cargo, he must pay him for as much cargo as would fill the space left empty in the ship, which is called the "*dead*" freight. If he has agreed to pay a certain sum, however,—called a "lump sum"—for the use of the ship, it is not material to the shipowner what empty space is left, provided that his ship is so loaded as to be seaworthy. It is not necessary that the whole cargo should be the actual property of the charterer, but he may allow others besides himself to use part of it. Indeed, he may advertise her to load as a "General ship," that is, to convey goods for third parties to the port or ports for which he has chartered, provided he keeps within the terms of the Charter Party.

Finally, it should be noted that a Charter Party is liable to a







# STEAMER

A

# Charter-Party.

LONDON, Jan. 8th, 19..

Stamp  
6d.

IT IS THIS DAY MUTUALLY AGREED BETWEEN *Morning Steamship Co., Ltd., Owners* of the good Steam Ship called the "*Sunrise*" of the measurement of 1,500 Tons Nett Register, 2,700 Tons dead weight cargo capacity guaranteed, classed 100 A 1 Lloyd's or equal thereto, now *lying at Valencia* and *Jones Jones & Co., of Liverpool* Charterers, THAT the said Steamer being tight, staunch, and strong, and in every way fitted for the voyage shall with all convenient speed, sail and proceed to *Liverpool* or so near thereunto as she may safely get, and there load, always afloat, from the Factors of the said Affreighters, a full and complete cargo, consisting of lawful merchandise, which the said Affreighters bind themselves to ship, not exceeding what she can reasonably stow and carry over and above her Tackle, Apparel, Provisions, and Furniture; and being so loaded shall therewith proceed as ordered on signing Bills of Lading to

*Bombay,*

or so near thereunto as she may safely get, and deliver the same, always afloat, on being paid Freight as follows :—

*Twenty-two shillings per ton,*

being in full of all Port Charges and Pilotage as customary.

1.—The Freight to be paid at Port of Discharge on unloading and true delivery of the Cargo in Cash at current rate of exchange.

2.—As much Cash as Master may require for Ship's ordinary disbursements at Port of Loading, not exceeding £30 to be advanced (if required), subject to 3 per cent. for Interest and Insurance.

3.—Merchants have the full range of Vessel's holds, including cross and half-deck bunkers, if any, and right of shipping Cargo on deck (at their risk), in so far as compatible with Steamer's seaworthiness.

4.—*Five* days, Sundays, and holidays excepted, are to be allowed the said Merchant (if Ship be not sooner despatched, Charterers having liberty to load up to midnight) for loading and discharging, but time occupied in shifting ports not to count, and ~~two~~ days on demurrage over and above the said laying days at *three* pence per nett register ton per day. Lay days in each port to count from Captain's notice of readiness for loading and discharging. Charterers to have option of loading and discharging on Sundays and holidays, such days to count as lay days for time actually occupied.

5.—The Act of God, perils of the sea, fire on board, in hulk or craft, or on shore, barratry of the Master and Crew, enemies, pirates, and thieves, arrests and restraints of princes, rulers, and people, collisions, stranding, and other accidents of navigation, excepted, even when occasioned by negligence, default or error in judgment of the Pilot, Master, Mariners, or other servants of the Shipowners. Not answerable for any loss or damage arising from explosion, bursting of boilers, breakage of shafts, or any latent defect in the machinery or hull, not resulting from want of due diligence by the Owners of the Ship, or any of them, or by the Ship's Husband or Manager.

6.—The Ship has liberty to call at any ports in any order, to sail without Pilots, to tow and assist vessels in distress, and to deviate for the purpose of saving life or property.

7.—The Cargo to be brought to and taken from alongside the Ship at Merchants' risk and expense.

8.—The Captain to sign Bills of Lading as presented, if in accordance with Mate's receipts, and at any rate of Freight, without prejudice or reference to this Charter-Party, if not at variance therewith, the owners having a lien on the Cargo for Freight, Dead Freight, and Demurrage. Should







stamp duty of 6d., which should be paid by affixing an adhesive stamp.

**Bill of Lading.** When goods are placed on board a "General Ship," a Bill of Lading is employed. The Bill of Lading is regarded as the captain's or the shipowner's receipt for the goods. It begins with an acknowledgment that the goods have been shipped, and undertakes that (certain perils excepted) they shall be delivered in a fit condition at the destination named.

The Bill of Lading carried on board the vessel is a duplicate of the document given by the master to the shipper of the goods at the time of the shipment. It specifies the name of the shipper; the date and place of the shipment; the name and destination of the vessel; the description, quality, and destination of the goods; and the freights which are to be paid.

When the ship arrives, the holder of the Bill of Lading is entitled to the possession of the goods. This is presented to the captain or ship's agent, who then gives permission for the goods to be handed over to the owner. Moreover, the ownership of the goods may be further transferred by the mere endorsement of the Bill of Lading.

Hence, it may be said that a Bill of Lading is the captain's acknowledgment that he has received the goods on board on the terms and conditions expressed therein; whereas a Charter Party is an agreement for the loan or hire of a ship, and conveys no title whatever to any cargo.

**Freight Rates.** The rates of freight for the outward journey are charged according to tariff. In this, the goods are arranged in classes, which are based chiefly upon the value of the goods, a higher rate of freight being charged for those of higher, than for those of smaller, value. The freight may depend upon the weight of the goods or upon their cubic capacity. Light or bulky goods are usually charged according to measurement, a ton of shipping being regarded as 40 cub. ft. In the case of heavy goods, the ordinary ton of 20 cwts. is taken.

A freight ton, however, is a very variable measure. In some trades, it is calculated at 50 cub. ft., whilst in the case of certain imports, the weight of a "ton" is made to vary. For example, a freight ton of rice is 20 cwts.; while a freight ton of pepper, which has less weight for the same bulk, is 11 cwts. These variations are always expressed on the Bill of Lading, and it is,



therefore, quite easy to examine the "freight notes," which are rendered either for import or export goods.

Precious metals, coins, valuable jewellery, etc., are carried at a rate which is based upon their value (i.e. about  $\frac{1}{2}$  to  $2\frac{1}{2}$  per cent.). Explosives and other dangerous objects are either not accepted, or carried under special terms and conditions.

For the return journey, the rates of freight are more often a matter of agreement between the shipping agents and the consignor. It is sometimes based on a measurement ton of 40 or 50 cub. ft., according to the nature of the goods; upon the ton weight; and often per quarter, which is then determined according to the quality and nature of the goods. Thus, wheat and maize may be calculated at 480 lbs. per quarter, 256 lbs. in the case of oats. For cereals from America to Liverpool, the freight is usually charged in pence per bushel, which is taken as equivalent to 60 lbs. Freight rates for timber are usually expressed per *standard* (i.e. for 165 cub. ft.).

**SHIPPING AND THE STATE.**—The predominant position of British shipping in the world in pre-War days was attained as the result of sustained initiative and self-reliance of the individual shipowner. Since the War, however, national control and State support have found such definite and widespread expression in the shipping policies of foreign maritime countries, that the British position in the carrying trade of the world has suffered a serious reverse. The *causes of the difficulties* of the British shipping industry are numerous. Chief among them are the decline in international trade; high running costs as compared with foreign shipping due to the higher wages paid and to restrictions from which competitors under other flags are exempt; and the activity of foreign Governments which, by subsidies and in other ways, have stimulated uneconomic competition for the transport of a diminished volume of trade. All classes of shipping have been affected, but the hardest hit have been the *tramp steamers*, since the liner companies can, to a certain extent through the conference system, protect themselves against the worst effects of rate cutting. The question has therefore arisen in an acute form in recent years: Can the unaided efforts of the British shipowner continue for any further appreciable length of time to cope successfully with foreign competition, now that the latter is so determinedly buttressed by State support?



The paramount need of British shipping, as of all shipping, is the restoration of world trade by the removal of restrictions and uneconomic practices, including subsidies. An attempt was made at the World Economic Conference in 1933 to secure international agreement to this end, but the attempt failed. Parliament was, therefore, led to pass the British Shipping (Assistance) Acts, 1935-7, which provided an annual subsidy not exceeding £2 million for the purpose of helping the owners of vessels registered at ports in the United Kingdom to compete with foreign shipping in receipt of subsidies from foreign Governments.

On 28th March, 1939, proposals for extending the subsidy scheme were announced in the House of Commons on the lines of that which had previously been in operation, but with some alterations as a result of adopting a five-year period instead of an annual basis. The sum of £2,750,000 a year was to be made available for tramp shipping, including vessels in the deep seas and near trades, but not the coasting trade. In each year the amount of subsidy will be subject to an arrangement for determining by reference to the index number of shipping freights whether subsidy should be paid in full or otherwise. Conditions will be attached to the subsidy, similar to those attaching to the previous subsidy, regarding employment of British crews and compliance with the National Maritime Board Agreements, where applicable.

In the liner section of the industry, an Advisory Committee is to be set up for an experimental period of two years, to examine requests for assistance from liner companies whose services are endangered by subsidised foreign competition, and to advise the Government accordingly. Parliament will be asked to make provision to enable the Government to grant financial aid promptly in cases where it has been decided that such assistance is necessary.

The recent proposals also include provisions for fitting the British Mercantile Marine to take its vital part in national defence; and financial arrangements for a fresh beginning with the building of merchant ships in this country, which has been dwindling rapidly, since, owing to the effects of rearmament, prices rose to levels that made construction prohibitive in the prevailing poor state of the freight markets.

As a condition of making the subsidy available, the Government will expect the shipping industry to do its utmost to promote



international measures tending to adjust the supply of tramp tonnage to the demand so as to safeguard the level of freight rates. The industry will also be expected to organise itself so as to satisfy the Government that at the end of the subsidy period it will be in a better position to maintain itself without Government assistance.

### TEST PAPER LVIII

1. To what extent and in what direction are the conditions of ocean transport different from and similar to the conditions of land transport?

2. Enumerate three important highways of ocean commerce, and describe the nature of the trade which passes over each of them.

3. Into what main classes may British shipping be divided?

4. What are the purposes for which shipping conferences are organised? Explain the methods employed to make the decisions of the conferences effective.

5. Ocean transport services may be divided into three types? Describe briefly the services fulfilled by each type.

6. Describe three different types of cargo steamers, stating for what trade or trades they are most suitable.

7. "On the ocean, as on the land, charges for the carriage of heavy goods in bulk are governed mainly by the costs of the services rendered; while the charges for quick transport at fixed times are in great measure adjusted to demands for services rendered." Discuss the reasons for fixing ocean freights according to the above principle.

8. What are the necessary contents of a Charter Party?

9. What recent legislation has been introduced for the benefit of the Tramp Shipping Industry? What is the object of this legislation?

10. Consider the effects of the modern specialisation of ships on the shipping industry and overseas trade.

11. What is a bill of lading? Explain its importance in respect of the carriage of goods and of a sale of the goods. Is it a negotiable instrument?

12. What are shipping conferences and how do they seek to control ocean freight rates?



## CHAPTER LIX

### MARINE INSURANCE

**INTRODUCTION.**—Insurance is a contract either to indemnify against a loss which may arise upon the happening of some event, or to pay on the happening of some event a sum of money to the person insured. Contracts of Marine and Fire Insurance are contracts of indemnity (i.e. compensation is given to the person insured for the loss he has actually suffered) ; that of Life Insurance, on the other hand, is an absolute undertaking to pay, in consideration of the premium, a sum of money on the death of, or attaining a certain age of, the person insured.

In the nature of things, insurance cannot prevent risks of loss to any appreciable extent. It is not a preventive save quite indirectly and in a very limited number of cases ; but it is rather in the nature of an arrangement by which a loss instead of being borne by one person may be spread over a large number of persons, until it becomes practically imperceptible.

Almost every risk to which man is liable may be insured against, although the more common forms of insurance are Marine, Fire, Life, Accident, Burglary, and Fidelity Insurance.

**MARINE INSURANCE.**—In all probability, the oldest form of insurance is that against risks which are likely to occur during sea transit (i.e. Marine Insurance). It is an arrangement by which one party agrees to compensate the owner of a ship or cargo for complete or partial loss or destruction at sea. The person so agreeing is called the underwriter, since he writes his name under the policy in which he has guaranteed to pay a certain sum in the event of loss.

**Lloyd's.** The establishment called “Lloyd's” is an association of underwriters and other persons engaged in marine insurance. It had its origin in a coffee-house kept by a Mr. Lloyd, which was the resort of persons interested in shipping matters, and for whose benefit the proprietor—long before the days of the electric telegraph—had established means of obtaining shipping news, not only by semaphore telegraphs from the coast, but by correspondence from all the places of trade throughout the world. The



spirited proprietor of the old-fashioned coffee-house is now perpetuated in the world-wide celebrity of the institution, which is unique in its facilities for obtaining news which relates to the shipping, not only of the United Kingdom, but of all other countries. There is scarcely a port of any importance where there is not an "agent for Lloyd's." It is his duty to furnish to the central establishment, lists of all ships arriving at and departing from the place he represents. Information is also furnished in respect of ships passing the port where he is stationed, together with the names of the places between which they are making their voyages. This and other information the masters of ships are willing and anxious to supply, in order that they may be reported for the benefit of their owners. This is managed by signal flags during daylight, and by signal lights at night. Lloyd's agents are also expected to do what is in their power to protect the interests of the members of Lloyd's. Since they are always selected from the best and most reliable shipping agents or merchants, the interests of shipowners, merchants, and underwriters are always considered safe in their hands.

Lloyd's subscription rooms are situated in Leadenhall Street, and comprise both public and private rooms. To the latter, admission is obtained by membership and subscription, only members having the privilege of carrying on underwriting business. Subscribers, however, are admitted to the rooms where the latest shipping and other news is always posted, and where they can also have access to a well-furnished and well-provided reading room. It is in the subscription room that a very large proportion of the business of Marine Insurance is done, and the method of procedure will now be treated.

**METHOD OF PROCEDURE.**—All insurances at Lloyd's are effected through the medium of brokers, who receive their remuneration not from the merchants for whom they act, but from the underwriters, in the form of a reduction of 5 per cent on the premiums they arrange to pay. The course of business is for the broker to write on a *slip* the particulars of the insurance he desires to effect, viz.—

- (1) Subject matter insured, i.e. ship, freight, or cargo.
- (2) The name of the carrying steamer or other conveyance.
- (3) The voyage or period of time or both, as the case may be.
- (4) The risks insured against.



When the goods are insured "F.P.A.," the risk taken by the underwriter is considerably reduced, since he is not liable for any damage or injury to them, but only for Total Loss and General Average Loss, the owner of the goods taking any risk of damage, and, in addition, loss or damage attributable to special causes mentioned in the F.P.A. Clause.

If the value of the goods is named on the slip and policy, the latter is known as a "*valued*" policy. If not, it is known as an "*unvalued*" policy; and in case of a claim arising under it, the value of the goods insured must be proved.

His slip having been arranged, the broker writes upon it the premium he is willing to pay, or presents the slip without any premium named to one of the underwriters with whom he is willing to do business. In this case, the latter fixes the price per cent. at which he is willing to undertake the risk offered to him.

The next step is for the underwriter to note on the slip the share of the insurance he will take. As a rule, it is seldom that one underwriter will take a larger sum, or "*line*" as it is called, than £300, since it is desirable that the risks be distributed as widely as possible. It is clear that it will be less risky for the underwriter to subscribe £100 on each of one hundred policies than £500 on each of twenty policies. Hence, the most frequent risks undertaken are for £100, larger "*lines*" being subscribed only on extremely good risks.

The "*slip*" having been started, the broker proceeds to pass it to other men of his circle. These, in their turn, note the "*lines*" they will take, and add their signatures. This process goes on until the amount required is made up. If the broker is unable to get the full amount subscribed at Lloyd's, he may offer the balance to one of the Marine Insurance Companies.

#### DIFFERENCE BETWEEN "HULL" AND "CARGO" INSURANCE.—

The chief forms of risks insured against are—

- (1) Hull Insurance (i.e. the vessel itself).
- (2) Cargo Insurance.
3. Freight Insurance.

One of the principal differences between the insurance of goods and that of ships is that, whereas the owner of a consignment of goods is at liberty to insure it for its full value, including a reasonable profit, the owner of a ship is more or less under compulsion to take some part of the risk upon himself. The reason



why underwriters are loth to insure a ship for her full declared value is not difficult to see. The owner of goods has no interest in over-insuring, since his actual control over the goods ceases as soon as they are shipped. This is not the case with a ship, since she is always under the control of the owner and his servants. A dishonest and unscrupulous owner of an old and unseaworthy ship, if no check were laid upon him, might effect a heavy over-insurance on the chance of her being lost, even if he did not directly connive at such a disaster.

Another point is that the underwriters are largely dependent upon information supplied by the *insurer* in the case of goods, but are *themselves* able to form a good estimate as to the value of a ship. Out of "Lloyd's"—the home of underwriters—there has arisen another institution known as "**Lloyd's Registry of British and Foreign Shipping.**" This establishment issues annually to its subscribers a book called the "Register Book," which contains a complete list of all ships registered in the British Isles, and of most foreign ships. In regard to each ship, particulars are given concerning—

- (1) The date and place of construction.
- (2) The materials she is built of.
- (3) Dimensions and registered tonnage.
- (4) The quality and condition of the ship.

**EXAMPLE OF A "HULL" INSURANCE.**—Suppose it is desired to insure the s.s. *Cornubia*, a vessel trading in grain on the West Coast of England. The owners of the vessel are Hamer & Co., residing in Cornwall.

The procedure followed in effecting the insurance of the vessel would briefly be as follows—

- (1) The shipowners, Hamer & Co., approach Messrs. Ashton, Brown & Co., Ltd., Marine Insurance Brokers, and request them to submit a quotation for a twelve-months' policy (i.e. a time policy).
- (2) The brokers interview the underwriters and get their "lines" written upon the slip. (See specimen on page 741.)
- (3) The underwriters' quotation is dispatched to Hamer & Co. by the brokers.
- (4) The terms being suitable, the shipowner instructs the broker to "place the insurance."
- (5) The insurance having been placed, the brokers forward a



# MARINE INSURANCE "SLIP"

## A. B. & Co., LTD.

R D.C., (Cross liab., Sister Ship,) add "and/or Charterers" No Thirds, F.G.A.,  
Y.A., av. ea. val., Devn. Contn. Negl. Clauses,  
Add "Sunk, on fire, or in collision."

*"Cornubia"*

*12 Mos. @ 1 Jan'y. /14. G. M. I.*

*Hull, Machy. etc.*

*vd. £100,000*

*Inst. hull cls. twts*

*50/=*

<i>10.000</i>	<i>Comm. Un.</i>
<i>10.000</i>	<i>R. Ex.</i>
<i>20.000</i>	<i>Marine</i>
<i>10.000</i>	<i>U. &amp; Canton</i>
<i>10.000</i>	<i>Indty</i>
<i>10.000</i>	<i>L &amp; P</i>
<i>10.000</i>	<i>World</i>
<i>10.000</i>	<i>Morten</i>
<i>1.000</i>	<i>F. W. M.</i>
<i>5.000</i>	<i>Tyser</i>
<i>4.000</i>	<i>P. Janson</i>

Opened *23/12/19* No. ....  
Closed *5/1/19* £ *100.000* .....



# COVER NOTE

ASHTON BROWN & CO., LTD.  
Insurance Brokers

Telegraphic Address  
ASHTON STOCK, LONDON

Telephone Nos  
575 AVENUE  
577 AVENUE

Cornhill,

London, 2nd. Jan'y, 19

Messrs. Hamer & Co.,  
Hayle.

Dear Sir,

We beg to advise having effected  
the following Insurance on your account.....

£ 100,000.

by the *Cornubia*

at and from *12 Mos. at 1 Jan'y '14. S.M.I.*  
to.....

including risk of craft  
on *Hull Machinery etc. wd £100,000.*  
*Institute Hull cls. & wtd.*

£100,000 at *50/* per cent. £.....  
Policy.....

*uprs as per slip*

£.....  
E. & O. E

Ashton Brown & Co., Ltd.

*J. Ashton*  
Director

WARRANTED FREE OF CAPTURE SEIZURE AND DETENTION, AND THE CONSEQUENCES THEREOF OR ANY ATTEMPT THEREAT, PIRACY EXCEPTED, AND ALSO FROM ALL CONSEQUENCES OF HOSTILITIES OR WARLIKE OPERATIONS, WHETHER BEFORE OR AFTER DECLARATION OF WAR.

WARRANTED FREE OF LOSS OR DAMAGE CAUSED BY STRIKERS LOCKED OUT WORKMEN OR PERSONS TAKING PART IN LABOUR DISTURBANCES OR RIOTS OR CIVIL COMMOIONS.

N.B.—CORN, FISH, SALT, FRUIT, FLOUR, AND SEED ARE WARRANTED FREE FROM AVERAGE, UNLESS GENERAL, OR THE SHIP BE STRANDED; SUGAR, TOBACCO, HEMP, FLAX, HIDES, AND SKINS ARE WARRANTED FREE FROM AVERAGE UNDER FIVE POUNDS PER CENT., AND ALL OTHER GOODS, ALSO THE SHIP AND FREIGHT, ARE WARRANTED FREE FROM AVERAGE UNDER THREE POUNDS PER CENT., UNLESS GENERAL, OR THE SHIP OR CRAFT BE STRANDED, SUNK, BURNED, ON FIRE, OR IN COLLISION.

GENERAL AVERAGE AND SALVAGE CHARGES PAYABLE ACCORDING TO FOREIGN STATEMENT OR PER YORK ANTWERP RULES IF IN ACCORDANCE WITH THE CONTRACT OF AFFREIGHTMENT



*Cover Note* to the shipowner. This "Cover Note" (see specimen) holds the shipowner covered until the policies are issued.

(6) The brokers having received instructions to issue the policies, they send the shipowner a "Debit Note" (i.e. a document similar to an invoice). (See specimen.)

**ASHTON, BROWN & CO., LTD.**

CORNHILL,

LONDON,.....6th January, 19.....

Debit Note for insurance effected for account of

Messrs.....*Hamer & Co.,*.....

.....*Hayle*.....

Vessel		Interest
..... <i>Cor nubia</i> .....	.....12 mos. @ 1st Jan. G.M.T.....	..... <i>Hull and</i> .....
.....	.....	..... <i>Machinery</i> ....
£100,000 @ 50s. %		£ s. d.
STAMP		2,500 - -
		25 - -
		<hr/>
		£2,525 - -
		<hr/>

(7) At the request of the brokers, the policies are issued. The whole of the amount underwritten at Lloyd's will be embodied in a single policy, whereas a separate policy is issued for each insurance company.

On the slips initiating the insurance of ships (as in those for goods), several abbreviations often appear, which should be noted, viz. "F.G.A.," "F.C.S.," and "R.D.C." These indicate respectively: "*Foreign General Average*," which implies that it is arranged between insurers and insured that, in the event of a General Average claim arising under the policy, the average settlement for which is made in a foreign country, that statement shall be adopted as the basis of settlement.

"*Free of Capture and Seizure*," which means that in case of war, the underwriters will not be liable for any claim for loss sustained through the ship being taken or attempted to be taken



as a prize of war. In times of peace, this clause is generally omitted. In war-time, or when there is a probability of war breaking out, underwriters insist on the insertion of the clause, unless they are paid an additional premium for "War Risks."

The last abbreviation signifies "*Running Down Clause*," and is printed on a slip of paper and attached to the policy. It contains an arrangement between the parties to the insurance that, should the vessel collide with any other ship and be found by a Court of law to be the wrong-doer, the underwriters will bear a part of the sum that the owners of the ship may be condemned to pay for damages and law costs.

**THE POLICY.**—The context of the present Lloyd's policy dates from the 13th January, 1779; the only modification since that date was in 1850, when the words "*Be it known that*" were substituted for "*In the name of God, Amen*"; and in 1874 the "Waiver Clause" [13] was added, which runs: "And it is especially declared and agreed that no acts of the Insurer or Insured in recovering, saving, or preserving the property insured, shall be considered as a waiver or acceptance of abandonment."

The memorandum at the foot of the policy [16] is older than the present policy; it was added in 1749 to the policy then in existence, and has not since been altered.

The form of a Marine Insurance Policy issued by Lloyd's is shown by the inset, and the student is recommended to make a careful study of this document. The figures in brackets in the policy have been inserted in order that reference may easily be made to some of the chief points of the document. These are—

[1] NAMES OF THE INSURERS, AND

[2] NAMES OF THE INSURED.

[3] LOST OR NOT LOST. This clause indicates that the underwriter agrees to indemnify the insured in the event of the vessel being lost, even if later it should be discovered that the vessel was lost prior to the insurance being effected, provided the insured was not then aware of the loss.

[4] DESCRIPTION OF THE VOYAGE OR PERIOD OF INSURANCE.

[5] NAME OF THE VESSEL.

[6] NAME OF THE CAPTAIN.

[7] TERMINATION OF THE INSURANCE FOR THE SHIP.

[8] TERMINATION OF THE INSURANCE FOR THE GOODS.











[9] **PERMISSION TO TOUCH AND STAY.** In the absence of any further usage, the clause does not permit a deviation of the ship from the course of navigation, except in the cases of special emergency (e.g. to avoid capture or to save human life).

[10] **VALUATION CLAUSE.**

[11] **NATURE OF RISKS COVERED.**

[12] **SUE AND LABOUR CLAUSE.** This clause gives permission to the assured, or his employees, to take all necessary steps in the preservation of the subject-matter of the policy when in danger ; and, further, the underwriter agrees to pay his share of any expenses which may be reasonably incurred in so averting or minimising a loss covered by the policy.

[13] **WAIVER CLAUSE.** The object of this clause is to protect the rights of the underwriter on the one hand, and those of the shipowner on the other, should they institute such measures as are provided for under the Sue and Labour Clause.

[14] At the time of the Hanseatic League, there resided in London a number of wealthy bankers from Lombardy, who were engaged in banking, but also undertook the business of insurance. They were the first English insurers who charged a fixed rate of premium. So great an impression did these Lombards make upon the commercial world, that their memory is still commemorated by the characteristic words at the end of a Lloyd's policy, viz. : " This Policy of Assurance shall be of as much Force and Effect as the Surest Writing or Policy of Assurance heretofore made in Lombard Street."

[15] **RATE OF PREMIUM.**

[16] Most policies, especially those signed by the insurance companies, bear the phrase " stranded, sunk, or burnt." In practice, this difference of wording has no effect.

[17] Many different views have been expressed as to the meaning of these initials. According to some, they represent the Latin words *salutis gratia* (i.e. for safety's sake) ; according to others, the words represented are *somma grande* (total sum insured) ; while it is also suggested that they signify the two words " Ship " and " Goods." This last opinion is confirmed by the fact that in an old policy dated 1708—preserved at Lloyd's—the letter and clauses referring specially to the " ship " are omitted.

Since the text of the Lloyd's policy does not contain all the



conditions, which vary according to circumstances, such as the route followed, the period of the year, etc., these matters are provided for by additional printed clauses, which are attached to the policy. These clauses vary according to the terms of the contract between the assurers and the insured. They are very important since they override the terms of the policy. Examples of such clauses are shown by the inset.

**COMPARISON OF LLOYD'S POLICY AND COMPANY POLICY.—**

Broadly speaking, there are two kinds of policies used in Marine Insurance. One is a Lloyd's policy and the other is a policy of an ordinary insurance company. The distinctive feature of the Lloyd's policy is that the parties assuring the whole of the policy against loss are very numerous. The assurers are not one body, but a great number of separate parties, and accordingly one finds a number of signatures upon a Lloyd's policy. (See Inset between pages 744-745.)

Each of these parties takes the risk for a stated amount appearing opposite his signature—the aggregate amount covered by all the signatures is said to be the amount of the policy; but it is important to bear in mind that the risk of the signatories, or underwriters, as they are called, is not a joint and several risk. Each is liable only for his own part; and accordingly, if there should be default on the part of one of the underwriters, the assured will lose a corresponding proportion in the event of his making a claim under the policy which is a good claim. He will not get payment in full. That, of course, is a drawback from the point of view of the policy-holder or the assured. On the other hand, it is an arrangement under which he is no doubt able to get his risks covered on more favourable terms. If each of the various underwriters had to be responsible for all the rest, at the very least he would want to charge, in addition to the premium covered by the policy, something further to cover the risk in case of default on the part of the other underwriters. It would increase the cost of the policy. It would also make it exceedingly difficult to get policies for large sums carried through at all. It would raise a question which at the present time has not to be considered at all, and would thus make it a much longer process to effect an insurance at Lloyd's. All that the underwriter has now to consider is whether he cares to undertake the risk, and for how







## STUCK.







much. If he were liable to his co-underwriters, he would have to consider what their standing was and whether he cared to guarantee them at all on any terms.

The ordinary insurance company, on the other hand, is a large body liable for whatever it undertakes, and all the risks under one policy of insurance are normally covered by one particular insurance company. Accordingly, if a very large risk has to be covered, it is either undertaken by one company, which promptly hedges by re-insuring a part of the risk with other companies ; or, alternatively, the assured has to take out more than one policy. Suppose it is a policy for £50,000. The first underwriter may take £10,000, the second £10,000, £5,000 the third, and so on, until the broker gets the amount covered that he desires, If he is working on those lines and a claim arises, the loss has to be borne between the assurers *pro rata* according to the amounts of their respective policies. If one company has undertaken the whole risk and has underwritten it, in the event of the claim arising the assured settles with the company he knows, and this company has to recover from the other companies with whom it has re-insured, so that they all lose *pro rata* according to the risks undertaken.

**PERILS OF THE SEAS.**—Primarily, the risks undertaken by the underwriter are for losses or injuries through the perils of the seas, including fire at sea or in port. They also include barratry (i.e. every form of unlawful dealing with the ship or her cargo by the master and crew), such as smuggling, privateering in war time, blockade running, and engaging in acts of piracy or anything else by which the owners could be defrauded.

Perils of the seas include Particular Average and General Average. It is under these two headings, and that of Total Loss, that almost all claims on underwriters are made—claims for loss by barratry and capture by enemies and pirates being very rare.

**PARTICULAR AVERAGE.**—Particular Average is loss occasioned through damage to the ship or the cargo, which is not for the benefit of all parties, or which has arisen through accident. Losses of this kind remain where they fall, and must be borne by the owners of the goods or by the underwriters. Such losses include those which arise from unavoidable causes, such as storms at sea, fire, or accident of any description, including collisions with



other ships, running ashore, springing a leak, etc. It is specially agreed between the insurers and the insured that no claim for loss by these causes, as Particular Average, shall be made, unless it amounts to 3 per cent on the value declared in the policy.

When insuring goods of large value or in large quantities, it is sometimes agreed to take each package, or each lot of an agreed number of packages, separately. In this case, if any one package, or part of any series of packages, is injured to the extent of 3 per cent on its declared value, a claim may be made for it (e.g. on a consignment of 20 bales Silk marked K. 1/20, valued at £1,200, to pay average separately on each bale valued at £60). This claim, however, could not be made if the 3 per cent was to be taken over the whole consignment. On some goods, it is necessary that the claim should amount to 5 per cent; whilst on others, no claim for particular average loss can be made at all. Goods of the former class are sugar, tobacco, hemp, flax, hides and skins; whilst the latter class includes corn, fish, salt, fruit, flour, and seed. The reason for these two classes of exceptions is that they are of a very perishable nature and peculiarly liable to spontaneous injury.

A claim for Particular Average is made out on next page.

The measure of the particular average loss is the difference between the amount realised for the goods concerned, in their damaged condition as they arrive at their destination, and the sum they would have realised had they arrived sound. In the example, these figures are £3,821 13s. less £3,176 2s. 6d. = £645 10s. 6d. Since the insured value of the 316 bales damaged by sea-water only amounts to £3,160, the actual value to be borne by the underwriters can be arrived at by a simple proportion sum as follows—

$$\begin{array}{rcl}
 & \text{Loss.} & \text{Loss.} \\
 \text{£3,821 13s.} & : & \text{£3,160} : \text{£645 10s. 6d.} : x \\
 & & \\
 & & 3,160 \times 645 \text{ 10s. 6d.} \\
 = \text{£} \frac{\quad}{3,821 \text{ 13s.}} & = & \text{£533 15s. 3d.}
 \end{array}$$

To this amount is added the extra charges made for adjustment, the total amount due for Particular Average loss being £590 5s. 4d.



**STATEMENT OF PARTICULAR AVERAGE on Cotton per "Queen Maud,"  
James Smith, Master, from New Orleans to Liverpool.**

*Insured*—  
840 Bales of Cotton, valued at £10 each, to pay average  
on every 10 bales running landing numbers . . . £8,400 - -

*Arrived*—  
808 Bales, of which 316 Bales were sea-damaged.

*Jettison*—  
32 Bales—paid by ship —. No claim.

	£	s.	d.	£	s.	d.
Insured Value of 316 Bales . . .	£3,160	-	-			
The same would have sold, if dry, as per Statement No. 1 . . .	£3,821	13	-			
Sales of 78 Bales, if wet, as pr. Statement No. 2 . . .	£614	6	-			
Do. of 238 Bs.—reped., as pr. Statement No. 3 . . .	£2,561	16	6			
	£3,176	2	6			
If £3,821 13 - —lose . . .		645	10	6		
then Insured Value £3,160 - - .					£533	15 3

**Extra Charges**

Broker's Survey . . . . .	2	2	-
Watches on Quay . . . . .	1	-	-
Extra Labour, Cartage and Canvas . . . . .	51	6	1
		54	8 1
		£588	3 4
Adjustment . . . . .		2	2 -
		£590	5 4

As soon as the goods are landed in a damaged condition from the ship, they are surveyed as quickly as possible by some competent and disinterested person, who certifies as to their damaged condition, and gives the cause for it as far as it can be ascertained. If the goods form part of a larger parcel, the amount of loss is easily ascertained by taking the average value of the sound part and comparing it with that of the damaged. If the whole of a parcel is injured, a certificate must be obtained from some expert person as to the sound value of such goods, and the amount of loss is settled on that basis. In some goods (e.g. sugar), a decrease in weight as well as in value will take place through their being damaged, in which case the owner is entitled to recover from the underwriters for both losses.

**GENERAL AVERAGE.**—General Average claims arise in another



form. The term signifies that the owners of the ship and cargo generally are liable to make a *pro rata* contribution towards any losses sustained or expenses incurred where other property or part of the ship has been sacrificed for the general good, and for the safety of the ship and cargo generally. In order that General Average may arise, there must have been—

- (1) A loss incurred intentionally ;
- (2) The avoidance of a danger common to the interests of all parties ;
- (3) An absolute necessity for some sacrifice to be made ;
- (4) The preservation of the ship and some proportion of the cargo ; and
- (5) No default on the part of the person whose interest has been sacrificed.

If a shipowner has in any way incurred expense or liability in saving from destruction, not only his own ship, but the merchant's cargo, it is only a matter of equity that he should be assisted in bearing this expense by all those who have benefited by the sacrifice made. For example, a ship is in a gale of wind, and is in danger of being cast on to rocks between her and the shore. The master enlists the assistance of a steam-tug, which is able, not only to keep her off the shore, but to tow her to a place of safety. The measure of remuneration to the steam-tug for such assistance is not the amount of time and labour expended as in an ordinary towage, but the value of property saved from destruction. The arrangement of the amount to be paid and the payment of it fall upon the shipowner, but he is entitled to recover a part of the sum so paid from the other interests concerned. These interests are generally three, viz.—

- (1) The ship.
- (2) The sum she is earning for freight on the voyage.
- (3) The cargo she is engaged in carrying.

Supposing the expense for towing amounted to £1,000, the ship being worth £ 9,000

the freight      1,000

the cargo      10,000

Total      £20,000



The expense would be borne as follows—

The shipowner  $\frac{9}{10}$  of £1,000 = £450

The freight  $\frac{1}{10}$  of £1,000 = £ 50

The cargo  $\frac{1}{2}$  of £1,000 = £500

Hence, between them these parties would bear the General Average Loss.

If the master of a ship deems it necessary for the safety of the property under his control to sacrifice any part of it, he is entitled to do so. For example, he may be obliged to cut away the ship's masts when she has been blown upon her beam ends, in order that she may be raised; or to jettison or throw overboard any part of the ship's cargo, so as to secure the safety of the ship and the rest of her cargo. In such cases, the shipowner may recover the loss as a General Average. Again, should the ship go ashore and it becomes necessary to lighten her to get her off again, cargo may be taken out in barges or boats and then put back again when the ship has been floated. The expense of this work, including the hire of barges, etc., would be recoverable as General Average.

General Average claims are nearly always mixed with claims for Particular Average. In the last instance quoted, for example, the ship might sustain some injury by going ashore—quite distinct and separate from the expense of getting her afloat again—which would be Particular Average. The same would apply to any claim for damage to goods forming part of the cargo which remained on board.

In connection with *General Average* it should also be noted that—

(1) Any person paying a claim for General Average, when goods are insured, is entitled to recover the amount he pays from his underwriters.

(2) The freight is always treated as a separate interest from that of the ship, although both may be the property of the same owner.

(3) In case of a claim, the master of a ship must justify any course of action he has taken by making a declaration called a *protest*. This declaration is made before a notary public, and sets forth all the circumstances of the case as recorded at the time in the ship's log book. This declaration must also be witnessed by at least two other members of the crew.

**EFFECT OF MARINE INSURANCE.**—The general effect of Marine



Insurance has been to reduce the likelihood of loss arising through the risks of the sea, because the underwriters have seriously considered the factors which tend to increase maritime risks; and have either charged prohibitive rates when unfavourable conditions existed, or refused to insure altogether. Anyhow, by the premiums they charged for covering the risk, underwriters have drawn the attention of the assured to the fact that there are some risks which need not necessarily exist, if some improvement be effected with regard to the property which is subject to the risk. In this way, money can be saved on insurance premiums.

### TEST PAPER LIX

1. Mention two forms of Insurance in ordinary use that are contracts of Indemnity against loss, and two forms which are not. State in each case the chief advantages of effecting such an Insurance.

2. What is the object of Marine Insurance?

3. What part has Lloyd's played in the history of Marine Insurance?

4. Describe the method of procedure in effecting an Insurance at Lloyd's.

5. Point out any difference between a "Hull" and a "Cargo" Insurance.

6. Say what you know of Lloyd's Registry of British and Foreign Shipping.

7. Enumerate the steps taken to effect a "Hull" insurance.

8. Explain the meaning of the following abbreviations—

"F.G.A.";

"F.C.S."; and

"R.D.C."

9. Give the meanings of the following terms used in Policies of Insurance—

(a) "Freight"

(c) Jettison

(b) Perils of the sea

(d) Lost or Not Lost.

10. Compare Lloyd's Policy with that of an ordinary Insurance Company.

11. Distinguish between a "General Average Loss" and a "Particular Average Loss." Why is the question of practical importance?

12. From the following particulars, draw up a statement of "Particular Average"—

(a) Sound value of goods, £326.

(b) Value in a damaged condition, £214.

(c) Insured value, £340.

(d) Charges in connection with survey, £5.

13. Under what circumstances may a general claim arise?

14. What three interests are usually concerned in the case of "General Average"? How is the amount of a liability for General Average ascertained?

15. State the effect of the introduction of Marine Insurance?

16. An insurance is sometimes spoken of as a pooling of risks. Explain this in relation to marine insurance.

17. Discuss from the point of view of the person insured and of the insurer—an insurance company, for example—the amount for which it would be prudent to insure a possession such as a house or ship or picture. On what reasonable grounds might an insurer object to the amount suggested, maintaining that it was too large, though the owner is willing and manifestly able to pay the premium?



## CHAPTER LX

### OTHER FORMS OF INSURANCE

**IMPORTANCE OF INSURANCE.**—Insurance has been defined generally as an entry upon a contract under which one party undertakes for a consideration to indemnify another against certain forms of loss; the risk of loss incurred by an individual being in practice shared or spread out amongst a large group. Insurance has become an indispensable adjunct to every form of activity in industry and commerce, and its importance increases year by year. Amongst the insurance institutions of the world, British companies stand high, and it is one of the characteristics of British insurance that it is transacted almost everywhere. The origin of the work was at home, but it was natural that, when new countries were being established overseas, British offices should insure materials dispatched from this country, should insure the buildings and works which were erected abroad against the perils of fire, and should cover the settlers in the new land against the risks which face them. Although in many countries insurance offices have now been formed on the model of the British institutions, the reputation of the latter has survived, so that all over the world British securities are still desired. At the present time the practice of insurance has become so general that almost every contingency which may arise as the result of accident or unforeseen circumstances may be covered.

**ORGANISATION OF AN INSURANCE COMPANY.**—There are many differences of organisation, not only between the various branches of insurance, but also between the undertaking engaged in the same line of business.

The insurance company is usually under the control of a managing director to whom are subordinated the managers both of the indoor and the outdoor staffs. Only in small-scale undertakings is it possible to combine these services.

*The Manager of the External Organisation* usually controls the out-door staff. In his task he is assisted by area superintendents and district inspectors, together with a corps of insurance agents, who are employed in the collection of contributions in specified areas. The agents may be subject to the direct control of the Head Office



or controlled indirectly through the superintendent of a particular town or district.

The out-door staff may be engaged in the procuring of life or accident insurance, or with the survey of risks in connection with fire insurance or certain classes of accident insurance. In the case of life assurance, the duties of the out-door representatives include the paying of visits to those who have inquired by letter on matters relating to life assurance—as it is often easier to explain such inquiries in the course of conversation than by correspondence—and also inducing a new customer to take out a policy. In some life offices it is customary for the collector to have a definite personal interest in the “book” which he collects, and to combine collection work with that of introducing new business and new customers, for which additional remuneration or commission is granted.

Fire and loss survey embraces perhaps some of the most interesting of the out-door work, including in the case of motor-car, plate-glass, or burglary insurance, inspection and report upon the proposal, or making some assessment of the equity of any claim on the spot, in the event of loss or damage.

The *Internal Organisation* supports the activities of the out-door staff through the *Publicity Department* by the insertion of suitable advertisements in newspapers, the drafting of circulars, and the forwarding of prospectuses and offers to interested parties.

The members of the inside staff are responsible for the preparation of the proposal forms of the prospective clients and for the ascertainment of the premiums. After drawing up the contract of insurance, the prospect is handed a statement containing the main terms and conditions. In close touch with the *Premium Department* is the *Actuarial Department* which calculates the probable risks which are to be covered, and the reserves to be set aside. If the risk is too great, then it must be distributed by means of re-insurance with other companies.

The settlement of claims begins as soon as an application for benefit is received. Acknowledgment and verification of the particulars of damage, the estimation of the loss incurred, and the amount of compensation to be paid to the insured are matters to be undertaken by the *Claims Department*.

The effect of these items on the capital and financial position of the undertaking is revealed in the *Accounts Department* where the



records are kept on double-entry principles. In the preparation of the Final Accounts consideration must be given to any special statutory regulations appertaining to the particular branch of insurance. Closely associated with the Accounts Department is the *Statistical Department*, especially in the large companies, which work with the aid of tabulating machines. The usual *Filing Department* and *Strong Room* are to be found, as well as the *Staff Department* and the *Audit Department*, both of which are closely related to the internal and external organisation of the undertaking.

The organic relationship existing between these various departments is seen from the following outline of business procedure—

- I. Before acceptance of the insurance proposal—
  - (a) Advertising, agents' propaganda, dispatch of prospectuses.
  - (b) Completion of inquiry forms; investigation of the circumstances which give rise to the risk.
  - (c) Assessment of the value of the subject-matter, agreement as to the sum to be insured, duration of the insurance, and other points.
  - (d) Fixing and communication of the premium.
- II. Subsequent to the acceptance of the insurance—
  - (a) Preparation of the policy.
  - (b) Re-insurance.
  - (c) Payment of the premium.
  - (d) Calculation of reserves and re-insurances.
  - (e) Modifications of the contract during the period of insurance.
  - (f) Renewal, or special reasons for terminating the insurance.
- III. Insurance Claims—
  - (a) Claimant's declaration of loss or damage.
  - (b) Salvage claims.
  - (c) Ascertainment of damage.
  - (d) Payment of benefits or compensation.
- IV. General administration—
  - (a) Ascertainment of general administrative expenses.
  - (b) Administration of the assets.
  - (c) Ascertainment and employment of profits and the payment of dividends.
  - (d) Preparation of returns for the Government authorities.

The characteristics of certain of the principal branches of insurance are discussed below.

**FIRE INSURANCE.**—Traces of practices related to fire insurance are to be found among the Anglo-Saxon Gilds; and doubtless the Curfew regulations of the Norman Kings, though largely inspired by motives of public policy, diminished private losses by fire. In its modern form, however, fire insurance has not existed in this country much longer than two centuries, and only spread to the Continent and to America at even later times. Fire insurance companies at the outset confined themselves as specialists to this class



of business; but they have gradually entered the field of Accident Insurance, and now usually combine all classes of risks. One of the most modern developments of fire insurance business is that known as "Loss of Profits" or "Consequential Loss" Insurance, whereby trading losses incurred as a result of the destruction of business or industrial premises by fire may be guarded against in consideration of an adequate premium.

To some extent, the same general principles apply to fire as to other branches of insurance; that is to say, the risk in respect of a particular building or the contents of a particular building can be covered by one policy, and the company covering it may re-insure with others, or the assured may take out several policies with different companies for the risk he desires to cover. Both methods are in general use.

Here, again, the cost of insurance, to some extent, depends upon the probability of the contingency insured against happening. Thus, the materials of which a building is constructed have a bearing upon the matter: a thatched building cannot be insured at the same rate as a tiled or slated building; but what is more important is the situation of the building—the nearness to other buildings; that is to say, the risk of the fire being communicated from outside, in addition to the risks of the fire arising in the property itself. Accordingly, in crowded neighbourhoods the rates tend to increase very considerably; and in practically all the cases some allowance is made in the cost of insurance for different kinds of approved preventive appliances, such as automatic sprinklers, fire alarms, the presence of a night watchman, the existence of fire-proof doors cutting up the building into fire-proof compartments, etc. To some extent, these safeguards are optional on the part of the assured. They need not be undertaken unless the insured wishes to get the benefit at lower premiums. But, to some extent, they may be necessary stipulations to get insurance.

**Effect of Fire Insurance.** The existence of fire insurance tends to reduce rather than increase the amount of loss accruing as a result of fire. Every year there is a certain amount of incendiarism (i.e. wilful setting fire to premises in the hope of getting money from the insurance company), but this, after all, is not important. As a rule, the amounts involved are quite insignificant



as compared with the very large sums covered by even a single large insurance company in the course of the year. Certainly, the original fire brigades in most countries were, in the first instance, due to the existence of fire insurance offices. The original fire brigades in London that were of any use whatever were actually owned by insurance offices, and there can be little doubt that they have encouraged a study of methods of construction tending to minimise the risks of big losses arising from fires in congested areas; and, through their influence in populous districts, efforts have been made to reduce the risks due to fire.

**LIFE ASSURANCE.**—This differs from other classes of insurance in providing an assured benefit in return for a fixed premium. In view of its certainty of benefit as compared with other forms of insurance, it is usually referred to as assurance, but usage varies. In England the earliest records of a life assurance is said to date from 1583, but in those days the object of the business seems to have been mainly the protection of the interests of creditors for definite short periods; as, for instance, the insurance of the life of a ship's captain while on a specified voyage. In modern times life assurance is a recognised means of thrift, and is resorted to either for the benefit of individuals, or as a means of family provision.

Most forms of life assurance are variations of two principal methods, "Whole Life" and "Endowment" Assurance; the first providing the payment of a stipulated sum at death only, the second arranging for this payment—in consideration of a higher premium—either at death or at the expiration of a stated number of years. It is necessary to bear in mind in regard to life assurance in particular that legislation in this country places some sort of limitation upon what might be called speculation in lives; that is to say, any contract of life assurance is void, unless at the time it was entered into, the assured—that is, the person who would benefit from the policy—had an insurable interest in the life assured.

For instance, A cannot effect an insurance on the life of B if B is a person in whose life he has no insurable interest. An *insurable interest* means that the relations between the parties must be such that A would suffer loss of some kind through the death of B.

This question of insurable interest is not confined to life insurance. As the object of insurance is to indemnify the assured against



loss, all insurances covering a matter in which the assured has no financial stake are in the nature of a gamble, and, as such, are illegal.

Apart altogether from life assurance as a provision for dependants—which is particularly useful to those who start in life without a very large capital—life policies have definite uses in connection with businesses in a variety of ways. Very often, if a man wants to borrow money, the risk that he may not live until he has repaid the loan is the most serious matter, and that is a risk which can be covered against by insurance. There are certainly cases where a business man could borrow, if one could be sure that he would live for a certain length of time. It may be that a person is borrowing on security of money coming to him under a contract, but the contract cannot be fulfilled by him if he dies. The insurance may cover the risk or the most serious part of the risk. Here the form of a life policy which will result in the payment of a specified sum if the borrower should die will provide a complete security for the loan.

Very often life policies are considered a most desirable arrangement in connection with partners. As a rule, on the death of a partner, his estate is entitled to receive fairly substantial sums of money from the surviving partner or partners. Until the surviving partner or partners can get a new partner to come in and take the place of the deceased, it may be that there is great difficulty in raising the money without crippling the undertaking. To surmount this difficulty, it is not an uncommon arrangement for the partners to insure each other's lives, or for them jointly to arrange to effect an insurance under which a specified sum is payable to the survivor on the death of the other.

**Effects of Life Assurance.** Prima facie, one would be inclined to say that life assurance cannot tend towards prolonging human life, but even here it is not so certain. Life assurance has not had a very marked effect in that direction, but it has probably had some effect. It is well to remember that the vast majority of life offices will not insure any life, but only *selected* lives (i.e. lives approved as a result of inquiry into hereditary conditions, family history, and into the state of health of the proposed at the time the proposal is put forward). Consequently, the medical examination which is necessary before the "life" is accepted,



may be the means of calling attention, in time, to an unsuspected weakness in the constitution of the person seeking the insurance; whereas without such examination medical advice would perhaps have been sought only at an advanced stage of the malady. But even supposing the existence of life assurance and its prevalence has not done much towards prolonging human life, it may safely be said that it has practically no effect in the opposite direction. Although there are cases in which men and women have been murdered or neglected for the sake of the insurance money, the amounts thus involved are very inconsiderable.

**ACCIDENT INSURANCE.**—This is of comparatively recent development. It received a great impetus from the Employers' Liability Act, 1880, which specified the limit of liability of employers in the case of accidents to their workpeople; and still further developments followed the Workmen's Compensation Acts of 1897, 1900, 1906, and 1925, the two last of which brought within their scope practically every employer of labour. The older Fire Offices extended their operations to deal with this class of business, and several new offices were expressly founded for the purpose. At the present time the chief kinds of accident insurance comprise Personal Accident, Workmen's Compensation, Motor Engineering, Plate-glass, Public Liability, Fidelity Guarantee, and Burglary Insurance.

**WORKMEN'S COMPENSATION.**—Employers are liable under certain Acts of Parliament to provide compensation to employees who have suffered damage through some form of injury connected with their work. Against this risk, the employer usually insures himself. This is a very suitable subject of insurance, since the risk of loss in the individual case is slight, and, therefore, the cost of insurance is not high; whereas, if a claim arises, it is very likely to be for an amount which is, at all events, worth considering. From the point of view of the insurer, it is a very satisfactory form of business, because it fulfils what is, perhaps, the most important qualification of all from the actuarial standpoint, that there should be an enormous number of separate risks undertaken, so that the experience of even a single year may represent a fair average experience as far as possible. Naturally, the smaller the number of risks, the greater is the likelihood that the experience as represented by the percentage of losses in any one year, or other comparatively short period, would fluctuate very widely, and that



makes for an unsatisfactory form of risk from the insurer's point of view, for it means very conflicting profits.

The effect of insuring against this risk of workmen's compensation from the employer's point of view, is that it is likely to be in the direction of improving conditions. That is to say, that the tendency will be for the insurer to be stricter in insisting upon safeguards than the legislature has been, as a condition for low rates from time to time.

In respect to the employee, the results are, perhaps, more doubtful. There seems to be some evidence to suggest that the fact that the employee will be compensated against losses arising to him through accidents occurring in pursuance of his employment, may tend towards making him more careless than he otherwise would be. A large number of accidents are due to the fact that the workers themselves will not take the precautions which the law requires to be taken by them, and it is quite possible that this state of negligence is not improved by the offer of monetary payments in case of accidents.

Employees can recover compensation even where the injury resulted from an accident for which no blame could attach to anyone. The employer will not, however, be liable if the injury is caused by the wilful misconduct of the injured employee.

**FIDELITY AND GUARANTEE INSURANCE.**—Another form of insurance which is fairly common, and which seems to be coming increasingly into use, is what is called Fidelity Insurance, under which the insurer guarantees the honesty of a stated person or persons, and agrees to recompense a named party against any loss he may suffer through dishonesty. Sometimes these policies refer only to the individual named therein; sometimes they cover the whole of the staff of the employer. It is important to bear in mind that insurance of this kind is strictly limited to insurance against loss arising through dishonesty; and it is a condition of these policies, in the ordinary way, that the insurer reserves the right to prosecute the party whose honesty is assailed, and has a right to demand the facilities for that prosecution from the employer.

The policy is not intended to cover losses due to the carelessness of the employer, and, therefore, it comes under a very different category and is a much safer risk. In the majority of cases, the



probability is that the risk is very slight indeed and in view of the fact that the premium ordinarily charged in this case is about 10s. per cent., it will be seen that it is expected that the proportion of claims will be low. Even at this low rate of premium, fidelity insurance is one of the best paying departments of a general insurance business.

An employer who has thus protected himself against a loss against dishonesty of the employees might grow careless about insisting upon reasonable precautions and risks of check; but, as a matter of fact, that is a question taken into consideration in considering the proposal for insurance; and unless there is some reasonable system of check, the proposal for fidelity insurance would not be undertaken at all.

**BURGLARY INSURANCE.**—A form of insurance which is very common in connection with certain classes of business is insurance against loss arising from burglary—sometimes burglary and house-breaking, and sometimes loss arising through the larceny of persons who have no right to be upon the premises. This is one of the most remunerative forms of insurance from the point of view of insurance offices, though a direct consequence of the owner being covered against the loss is that he neglects precautions which he would otherwise, in all probability, adopt (i.e. the risk of the event happening is, upon the whole, increased by the fact that the risk is covered by insurance).

There are many other forms of insurance in less general use than those already mentioned, among which may be mentioned insurance against bad debts, trade depression, against the occurrence of war within a certain time. It is also possible to insure against loss upon exchange; that is to say, to insure for an agreed sum in the event of exchange falling below a specified point—although that would be a wasteful way of covering a risk of that description. The simplest way of covering such a loss is to maintain a balance of liquid assets and liabilities in each of the countries between which remittances are made. For instance, suppose a business house in England buys goods in England and ships them to Brazil, so that in the latter country they are sold in Brazilian currency. The English house, however, looks for the proceeds to settle their account in England. In determining the satisfactory price to be paid in Brazilian currency,



it has to take into account the value of the Brazilian currency at the time, and to provide for an alteration in the exchange between the date when the sale was effected and the date when the remittance is made to England to pay the English liabilities. The best method is to purchase bills on the date of sale at the prevailing rates of exchange. In this way, the selling price can be converted at once into sterling ; and unless the bills purchased are afterwards dishonoured (which may be left out of account as a normal risk in connection with exchanges), they do not run any risk in connection with that particular deal.

**SOCIAL INSURANCE.**—A specialised branch often referred to comprehensively as Social Insurance is that dealing with losses due to sickness, disease, or unemployment, and provided for by State Insurance Schemes. Before the establishment of national systems of Health Insurance and Unemployment Insurance by statute, various well-known Benefit or Friendly Societies had come into existence for the purpose of securing their members against losses of this kind ; some of the Friendly Societies which were registered under the Friendly Societies Act, 1854, helped their members in seeking employment and made allowances to them in seasons of slack trade, among other benefits designed for the purposes of indemnifying their members against various forms of loss. Under the national schemes, the majority have become “Approved” Societies administering certain standard benefits within the compass of the national systems, while maintaining most of the distinctive features of their own scheme. Their membership is largely composed of those who prefer to pay premiums in small instalments at frequent intervals rather than in larger instalments over longer periods, or who could not in any event arrange to pay large premiums in a lump sum. For this class of contributor Industrial Life Assurance Offices have also come into being.

**National Health Insurance.** The scheme of National Insurance which came into operation on 15th July, 1912, but which has since been amended, provides for insurance against sickness of persons employed in manual labour if over the age of 16 and under 65, and affects persons other than manual workers if their remuneration does not exceed £420 per annum. Its objects are carried out by funds towards which employers, employees, and the State contribute in defined proportions. The employer is liable for the



payment of both his own and the employee's contributions, and is authorised to deduct from the remuneration paid the amount for which the employee is liable.

It is the duty of the employee to produce his contribution card to his employer when required, and he must deliver it up to his employer when required for stamping. The employer is required to stamp the employee's card with the amount of his own and the employee's contribution.

Persons liable for National Health Insurance are also liable for Pensions Insurance, whereby under the Widows', Orphans', and Old Age Contributory Pensions Act, 1925, a contributory scheme has been devised for providing pensions to the widows and orphans of insured people and the payment of old age pensions to insured men and their wives at age of 65.

**Unemployment Insurance.** Unemployment Insurance, which is governed by rules similar to those which apply in the case of National Health Insurance, is provided for by various Unemployment Insurance Acts. The scheme includes substantially all persons in respect of whom Health Insurance is payable, other than outworkers and private domestic servants. The payments are on a contributive basis. Owing to industrial depression and the need for the provision of additional benefits, the contributions have been increased from time to time.

Until recently it was commonly held that unemployment was not an insurable risk. There are, however, four requisites which a contingency must satisfy before insurance principles can be applied to it—

- (1) There must be a risk whose nature must be clearly specified.
- (2) To this risk large numbers must be exposed.
- (3) It must be a risk which appeals to those on whom it is likely to fall, as a menace against which they would, if they could, provide.
- (4) The risk must be capable of being calculated with some degree of certainty.

If, by unemployment insurance, we mean insurance of able-bodied men out of work for a definitely limited period, and that a test of willingness to work is provided, then the risk may be regarded as established. The second and third of the above requisites clearly apply to unemployment, since large numbers are subject to it and



many would be glad to provide against it. The statistics necessary to satisfy the fourth requisite are now provided by the returns of those in receipt of insurance benefits compiled by the Ministry of Labour.

The Unemployment Insurance scheme is operated by the State through the Employment Exchanges, which, in addition to paying the benefits under the Acts, also endeavour to find work for the insured person whose contributions to the insurance scheme cease during that period in which he is unemployed. The benefits are of two kinds: (1) "Ordinary," payable to the insured person, and (2) "Dependant's," varying in amount according to the number of persons dependent on the insured person. No benefit is paid if the worker has lost his work owing to a trade dispute at his place of employment, or to his own misconduct or voluntary cessation of work, or if he is benefiting under the National Health or the Old Age Pensions Insurance Schemes. As the Unemployment Insurance benefits are a charge on State funds, there is every inducement to transfer unemployed workers to those industries and districts where there is greater need for their services.

### TEST PAPER LX

1. Upon what circumstances does the rate of charge for Fire Insurance depend?
2. State in general terms what has been the result of the introduction of Fire Insurance.
3. Give an explanation of the term "Insurable Interest."
4. What, in your opinion, have been the effects of Life Insurance?
5. Explain the term "Fidelity Guarantee Insurance."
6. State in general terms what risks should, in your judgment, be insured against in any one of the following businesses, and what risks you think it would be best not to cover by insurance. Give your reasons in each case—
  - (a) A Stockbroker
  - (b) A Motor-car Proprietor
  - (c) A West Indian Merchant
7. Give an example of re-insurance on a Fire Risk.
8. Name a few of the safeguards which are commonly adopted with a view to securing a lower premium on a fire policy.
9. Should Fire Brigades be maintained by Insurance Companies? State reasons for and against.
10. What do you understand by a Joint-Life Assurance? Name a few cases in which such assurances are effected.
11. What is the unsatisfactory feature in connection with Burglary Insurance from the point of view of the Insurance Company?
12. What do you understand by "Insurance against Loss in Exchange"? Is this form of insurance common? Give reasons for your answer.
13. Give the meaning of the following abbreviations and explain three of them—

R.I.    Y.A.R.    F.p.a.    R.D.C.    P.p.i.    F.c.s.



# ABBREVIATIONS USED IN TRANSPORT AND INSURANCE

<b>A.R.</b> . . .	Against all risks	<b>H.C.</b> . . .	Held covered
<b>A.I.</b> . . .	First class	<b>I.O.M.</b> . . .	Isle of Man
<b>A.M.</b> . . .	<i>Assurance Mutuelle</i> (mutual assurance)	<b>I.W.</b> . . .	Isle of Wight
<b>A.P.</b> . . .	Additional premium	<b>I.H.P.</b> . . .	Indicated horse-power
<b>A/R</b> . . .	All risks	<b>Ince.</b> . . .	Insurance
<b>B/L</b> . . .	Bill of lading	<b>Instns.</b> . . .	Instructions
<b>B. Ch.</b> . . .	Bristol Channel	<b>In trans.</b> . . .	In transit
<b>b.t.</b> . . .	Berth terms	<b>ldg.</b> . . .	Loading
<b>Cont.</b> . . .	Continent	<b>L.I.P.</b> . . .	Life insurance policy
<b>c.f.</b> . . .	Cubic feet	<b>Ltdg.</b> . . .	Lighterage
<b>C. and D.</b> . . .	Collection and delivery	<b>L.C.</b> . . .	Label clause
<b>c.f.i.</b> . . .	Cost, freight, and insurance	<b>Min.</b> . . .	Minimum
<b>Cge.</b> . . .	Carriage	<b>M.D.</b> . . .	Millwall Docks
<b>C.i.f.</b> . . .	Cost, insurance, and freight	<b>M.M.</b> . . .	Mercantile marine
<b>Cld.</b> . . .	Cleared	<b>N.R.</b> . . .	No risks
<b>C/P</b> . . .	Charter party	<b>o.c.</b> . . .	Open charter
<b>C.R.</b> . . .	Company's risk	<b>Oc. B/L</b> . . .	Ocean bill of lading
<b>C.T.L.</b> . . .	Constructive total loss	<b>O.P.</b> . . .	Open policy
<b>Cub.</b> . . .	Cubic	<b>O.R.</b> . . .	Owner's risk
<b>C.C.</b> . . .	Continuation clause	<b>p.o.c.</b> . . .	Port of call
<b>d.l.o.</b> . . .	Dispatch loading only	<b>P.V.</b> . . .	<i>Petite vitesse</i> (goods train)
<b>d.w.</b> . . .	Deadweight	<b>P.A.</b> . . .	Particular average
<b>D/C</b> . . .	Deviation clause	<b>P.D.</b> . . .	Port dues
<b>D.f.</b> . . .	Dead freight	<b>P.p.i.</b> . . .	Policy proof of interest
<b>E.T.C.</b> . . .	Eastern Telegraph Co	<b>P. &amp; O.</b> . . .	Peninsular & Oriental Steam Navigation Company
<b>e. &amp; o.e.</b> . . .	Errors and omissions excepted	<b>regs.</b> . . .	Registered tonnage
<b>Frisco.</b> . . .	San Francisco	<b>R.I.</b> . . .	Re-insurance
<b>f.o.</b> . . .	For orders	<b>R.C.H.</b> . . .	Railway Clearing House
<b>f.d.</b> . . .	Free dispatch	<b>R.D.C.</b> . . .	Running-down clause
<b>F.O.B.</b> . . .	Free on board	<b>Schr.</b> . . .	Schooner
<b>F.O.W.</b> . . .	First open water	<b>Shipt.</b> . . .	Shipment
<b>F.T.</b> . . .	Full terms	<b>S.L.</b> . . .	Salvage loss
<b>F.a.a.</b> . . .	Free of all average	<b>S.N.</b> . . .	Shipping note
<b>F.a.s.</b> . . .	Free alongside ship	<b>S.W.I.D.</b> . . .	South West India Dock
<b>F.e.s.</b> . . .	Free of capture and seizure	<b>S. &amp; F.A.</b> . . .	Shipping and forward- ing agent
<b>F.f.a.</b> . . .	Free from alongside	<b>Thro' B/L</b> . . .	Through bill of lading
<b>F.g.a.</b> . . .	Foreign general average	<b>T.L.O.</b> . . .	Total loss only
<b>Fm.</b> . . .	Fathom	<b>Tonn.</b> . . .	Tonnage
<b>F.p.a.</b> . . .	Free of particular average	<b>T.B.</b> . . .	Tons registered
<b>Frt. fwd.</b> . . .	Freight forward	<b>U.K.C.</b> . . .	United Kingdom or Continent
<b>F.L.N.</b> . . .	Following landing numbers	<b>U/a</b> . . .	Underwriting account
<b>G.V.</b> . . .	<i>Grande vitesse</i> (quick goods train)	<b>U/w</b> . . .	Underwriter
<b>G.A.</b> . . .	General average	<b>W.P.</b> . . .	Without prejudice
		<b>W.O.B.</b> . . .	Washing overboard
		<b>Y.A.R.</b> . . .	York-Antwerp Rules
		<b>#</b> . . .	Numbers, or packages



## SECTION VII—WAREHOUSING

### CHAPTER LXI

#### FUNCTIONS OF WAREHOUSING

A **WAREHOUSE** is an establishment for the storage or accumulation of goods. Warehousing is one of the most important auxiliaries in the service of the trader, since by its means the necessity for delay in awaiting the arrival of goods from the producers is avoided. The chief functions fulfilled by this branch of commerce are—

(1) The removal of the hindrance of time which would otherwise be involved in obtaining possession of goods from the places of production.

(2) The regulation of the price of commodities by preventing the violent fluctuations which would result if such a store of goods was not accumulated.

(3) The provision of a market at which retail dealers and others may view the different commodities offered for sale.

For convenience of treatment, warehouses may be grouped into two classes—

(1) Public warehouses, chiefly located at the docks.

(2) Wholesale warehouses.

**PUBLIC WAREHOUSES.**—One of the most important developments which have been called into existence in the course of the last few hundred years is that of the warehouse which facilitates the turn-over of goods. In the Middle Ages, when the mercantile marine, accompanied by a convoy, safely landed its treasures, they had immediately to be taken into consumption. What the merchant was unable to dispose of was subjected to the influence of wind and weathers, and to the danger of theft. Long before the goods were brought into consumption, the duties had to be paid. Whether the market was flooded or not, irrespective of demand and supply, the merchant had to dispose immediately of his goods. It was, therefore, a great boon when the first public warehouse was erected in London in 1660. This example was soon followed by other English seaports, and similar warehouses were also established in all



the ports of the Continent, as well as in the most important trading centres of the interior. At the present time, these warehouses, especially at the large seaports as at London, Liverpool, Havre, Hamburg, etc., are equipped with the most remarkable conveniences. Standing room is afforded near them for both ships and railway wagons, and accommodation is provided for the huge stocks of goods to be sold on the world market.

**ADVANTAGES OF WAREHOUSING.**—The main advantages of warehouses may be summarised as follows—

I. They serve to safeguard the stocks of the merchant who has either no warehouse of his own or very limited warehousing space. Hence, he is not restricted in his business operations through lack of room.

II. They make provision for the unloading of incoming and the loading of outgoing ships, as well as for the goods brought by rail. Consequently, the warehouses are equipped with expensive technical appliances; powerful steam cranes are used for lifting the heaviest loads; grain and other commodities are landed from the ships by hydraulic means and placed into the warehouses or into other vessels standing in the docks. In this way, the expenses of loading and unloading are kept at a minimum.

III. The merchant is afforded the convenience of having his goods stored in close proximity to his selling area, thus enabling him to serve his customers most economically and at the smallest expense. For example, a merchant in London trading with Australia may direct his goods to be warehoused at different seaports in the North of England, near to his customers, instead of receiving them all in London. A considerable saving in freight and in time can thus be effected.

IV. There is no necessity for the payment of duties immediately on the importation of goods. But for the provision of bonded warehouses, the importer would have to pay the import duty on their entry into the country. In addition to the cost price of the goods and the freight, the importer would also have to lay out an enormous amount of capital as duty. It can, therefore, be seen that it is a great convenience for the importer to be able to warehouse his goods without being called upon to pay the duty immediately. Such payment would be necessary only when the goods are sold and are thus brought into consumption. This very



important service is rendered by means of *bonded* warehouses, which are conducted by private enterprise, though they are under the strict supervision of the State.

**BONDED WAREHOUSES.**—As the name suggests, these are warehouses with regard to the safe keeping of which the proprietors have entered into a Bond with the Customs authorities. The Bond is determined by various considerations, such as size, volume of trade, etc., and is drawn up by the Crown solicitor and the merchant or proprietor. Sureties are also required. Irregularities or fraud of any character are penalised by the cancellation of the Bond, and the consequent loss of the privileges which the Bond ensures.

**GENERAL.** In London, Bonded Warehouses are numerous, and distributed mainly around the wharves and docks. They may be roughly classified into the following groups—

- (1) *Vaults.* For warehousing wines and spirits of all descriptions.
- (2) *Tobacco Warehouses.* For warehousing and manufacturing tobacco (including cigars and cigarettes).
- (3) *Sugar Refineries.* For the refining of molasses, raw cane, and beet sugar.
- (4) *Coffee and Cocoa Warehouses.* For the warehousing and re-packing of coffee and cocoa.
- (5) *General Warehouses.* Warehouses for preserved fruits, and the various goods subject to duty other than those enumerated above.

As a general rule, warehouses are bonded for the warehousing of one class of goods only, although in many cases goods more or less similar, such as coffee, cocoa, and sugar, are allowed to be warehoused in the same warehouse, but not on the same floors.

**The Trade of London,** so far as Bonded Warehouses are concerned, is specialised. The following list shows the disposal of the main groups of dutiable goods—

- (1) *Tobacco*—
  - (a) Unmanufactured, Victoria Dock ;
  - (b) Cigars and Cigarettes, Cutler Street Warehouse (under the Port of London Authority).
- (2) *Wines*—
  - (a) Immediately on importation, London Dock ;
  - (b) Later, various Up-town Vaults around the Docks.



(3) *Spirits*—

- (a) Brandy, London Dock ;
- (b) Gin, London Dock ; (c) Later, in various Up-town Vaults ;
- (d) Rum, West India Dock.

Coffee, cocoa, and preserved fruits are warehoused in various warehouses, both in the docks and wharves, and outside. As a general rule, they are warehoused separately. No wines or spirits are warehoused in the Lower Docks, such as Royal Albert, Victoria, Tilbury, etc.

All Bonded Warehouses are subject to the supervision of the Customs officials, who remain, in almost every case, on the premises. They are also secured with Crown locks when closed.

**Operations in Warehouse.** When in the various warehouses, the goods are dealt with in such a way as to render them suitable for home consumption and export ; in every case the permission of the Customs is necessary, and application must be made on special forms provided for the purpose. The nature of the operations varies with the character of goods. Briefly, the procedure is as under—

(1) *Wines and Spirits.* Racking, i.e. removing the contents of one cask into another or several others. Bottling, i.e. removing contents of casks into bottles for home consumption.

(2) *Tea.* Blending and re-packing various teas, e.g. teas from China, India, or Ceylon are blended and re-packed into small packets for home use. At the present time the Customs duty on tea has been abolished.

(3) *Sugar, Coffee, Cocoa.* Refining and re-packing.

(4) *Tobacco.* Manufacturing and re-packing.

**TRANSFER OF OWNERSHIP OF WAREHOUSED GOODS.**—Warehouses also render other valuable services to trade. Among these may be mentioned the facility for transferring the ownership of warehoused goods. Just as the ownership of goods shipped by a certain vessel can be transferred by the endorsement of the Bill of Lading, so the goods stored in the dock warehouses can be so transferred. This is effected by means of a "Warrant." In this document, the warehouse authorities certify that they have received the goods stated thereon, and undertake to deliver the same to the bearer of the "Warrant," who is regarded as the legitimate owner. It is usually made out to "order" and is negotiable by endorsement.



On page 771 is a specimen "Warrant"—

The merchant who has warehoused his goods, or the person authorised by him, may reclaim them at any time. When reclaiming the whole of the warehoused goods, he must produce the warrant to the authorities, in return for which he receives the Delivery Order, which empowers the warehouseman to deliver the goods. If only a portion of the goods is required, the corresponding quantity is written off the warrant, which is then returned to the owner of the warehoused goods.

The holder of the warrant can also sell the goods by delivery of the warrant with his endorsement thereon, and the buyer can dispose of them in the same way. Thus, a consignment of goods represented by "warrant" may change hands repeatedly on the world market without being once moved from the warehouse.

It is therefore possible for the merchant to carry about in his portfolio the title to whole ship-loads of goods and to dispose of them by a mere stroke of the pen. Naturally the sale of goods against warrant presupposes an unlimited confidence in the warehouse authorities.

All goods which are warehoused must be insured against loss by fire, protected against theft, and preserved from deterioration. Goods which are unsuited for warehousing are not accepted, except under special conditions. The warehouse authorities are able to protect against all risks, except one, viz. a change in value consequent upon the fall in market prices. On the other hand, the warehouse offers excellent advantages for public sale. At many warehouses, especially in London and Amsterdam, public auctions have been established at which Colonial goods are periodically sold by authorised brokers. At these auctions, all the most important wholesale dealers attend, or are represented by their commission agents.

Warehouses are important not only to the importer, but also to the home manufacturer and exporter, since they offer a number of advantages to them in the conduct of their trade. Instead of accumulating his stocks of finished goods in his own warehouse, the manufacturer may prefer to place them at the disposal of the market by storing them in the warehouses of the chief trading centres. In this way, he has a better chance of selling them when the favourable moment occurs.



# Port of London Authority

Deck Lot

No. B 18153

ROTH 8974

Dated this 12<sup>th</sup> March, 1911

**Warrant** for Fifty Slabs Marble Master Jones  
 imported in the Onpheros entered by H. Smith & Co.  
 from Genoa deliverable to N. Robinson & Sons  
 on the 1st March, 1911  
 or Assigned by endorsement hereon.



Rent commences on the  
 and all other charges from the date of this Warrant.

17th March 1911

MARK	Lot NUMBERS Slabs		Net				WEIGHT.		MARKS		Lot NUMBERS Slabs		Net		WEIGHT.		
			Gross.		TARE.		TARE.				Gross.		TARE.				
	Original	Break	Cwt.	qrs.	lbs.	Cwt.	qrs.	lbs.	Original	Break	Cwt.	qrs.	lbs.	Cwt.	qrs.	lbs.	
H.T.J.	1	5	8	3	16						1	5	9	2	4		
		5	9	1	4							5	3	8			
		5	10	2	3							5	3	15			
		5	9	1	5							5	2	5			
		5	8	3	17							5	3	1			
			46	3	17							46	2	5			

Ledger A F<sup>o</sup> 289  
 E. Brown Clerk. J. Simpson Warrant Clerk.



To the various services rendered by the warehouse to the importer and exporter, as well as to the manufacturer, should be added the facility offered for the hypothecation of the goods; that is to say, while still retaining the ownership of the goods, the merchant might pledge the warrant, in order to raise a loan. It is very important that merchants and manufacturers should thus be able to hypothecate their stocks for, by so doing, the former, in times of crisis, can meet their obligations out of the loan thus raised, whilst the latter can continue their productive operations instead of having to discharge their men.

**WAREHOUSES UNDER THE PORT OF LONDON AUTHORITY.**—It is estimated that about 60 per cent of the shipping entering the Port of London discharges in the docks; whilst the rest discharges at wharves or at moorings in the river. From vessels which go into the docks, a large portion of the cargo is taken away by lighters, which have, by statute, the right of free access to the waters of the docks. Another portion is discharged on to the dock quays for conveyance to its destination by land; while yet another part, not intended for immediate consumption, goes directly into the warehouses of the Port of London Authority. This warehousing business is of great importance, comprising, as it does, every class of goods entering the port. The principal are grain, timber, wool, frozen and chilled meat, sugar, tea, wines and spirits, and tobacco. The whole of the tobacco warehoused in London is stored with the Port Authority.

As a body, the Port of London Authority are neither growers, producers, nor importers of produce, but simply custodians who perform such operations as the owner of the goods may direct. They house the produce discharged from vessels, and report upon its weight, quality, and condition to the merchants interested.

The Authority is the greatest warehousekeeper in the world; its operations range from the simple service of merely allowing goods the right of passage through its sheds to the most complicated examination and manipulation of products of all kinds. All the services required by merchants are performed by the Authority's staff who require years of training and experience to qualify them for their work. The services rendered by the Authority include, besides the safe custody of the goods, all the operations required by the merchant in the course of marketing, sale, and delivery of his



goods. These operations are often various and responsible. The catalogues issued by the brokers, describing the goods offered by them for sale, are prepared from descriptions of the quality and condition, weight, and other essential particulars required to be known by the buyer, furnished by the Authority's staff; whilst the grading and letting of the goods in a way suitable for the market is also done on their advice. Samples to show indications of the bulk have to be drawn and in such goods as rubber and fibres the judgment of the expert is necessary. The examination for damage to goods in order to ascertain liability as between the parties interested is another duty demanding not only skill but the strictest impartiality, and perpetually the Authority is placed in the position of an arbitrator between buyer and seller. By the issue of the dock warrant to merchants, the Authority affords facilities for financing commercial operations, and by its arrangements with the fire insurance offices the warehouses are rendered immune from fire. The weighing and measuring of the goods, the separation of damaged from sound goods, and the making merchantable of salvage goods, are amongst the operations conducted as part of the everyday routine work in the warehouses. The services of the Authority as warehouse-keepers are supplemented by that of carriers in that they undertake the collection and delivery of goods to and from the domicile of merchants and manufacturers, employing for this purpose railway, lighterage or cartage facilities enjoyed by them at their docks and depots.

#### TEST PAPER LXI

1. What are the functions of a warehouse?
2. Mention two classes of warehouses.
3. Summarise the main advantages of *public warehouses*.
4. What are Bonded Warehouses and for what purpose are they used?
5. Show to what extent specialisation has arisen in the sphere of warehousing.
6. Why are Bonded Warehouses under supervision of the Customs authorities?
7. How may the ownership of warehoused goods be transferred?
8. Compare a public warehouse with a market.
9. What is meant by the hypothecation of warehoused goods?



## CHAPTER LXII

### WHOLESALE WAREHOUSING

**THE WHOLESALE WAREHOUSE.**—The wholesale warehouse is chiefly concerned with the purchase and sale of commodities ; and for the conduct of this work in the most profitable manner, special ability is required which consists chiefly in the power to utilise the existing market phenomena with care and dexterity, the possession of business tact, a grasp of the prevailing conditions with reference to the supply of goods, insight into the character of buyers and sellers, as well as high moral qualities combined with a store of physical and mental energy on the part of the organiser.

**NECESSITY FOR GOOD ORGANISATION.**—It has been seen that organisation is, in reality, the art of splitting up work into more or less water-tight compartments, so that each person may do his share independently of the rest. The scope of the duties of the various individuals is limited, so as to enable them to reach a higher stage of perfection ; and it is the business of the organiser to see that this division into compartments is arranged on such lines as will make for efficiency.

It is the organiser's duty to see that he has a good design for the business ; and the function of the management is to see afterwards that the idea behind the design is not lost sight of, and that the scheme is being carried out in accordance with the original intention.

Good organisation as a starting-point is clearly desirable for the successful conduct of a wholesale warehouse, but it is useless if it is not accompanied by efficient management. It is only in quite a superficial sense that business organisation can be regarded as the art of cutting matters up into water-tight compartments. In a sense, each department of a wholesale business has to be separate and distinct ; but it must be remembered that the mere separation of the different departments serves no purpose in itself, but is merely a convenience to indicate to the different members of the staff the limitations of their respective duties, so as to avoid overlapping. Nothing can be less likely to lead to good results



than the building up of a system of organisation under which persons in one department have no knowledge of what is being done in other departments and have no means of communicating with each other. In reality, all the different departments of the business are simultaneously at work to produce combined results, and unless they are able to work together nothing can be gained, but a great deal can be lost as a result of such organisation.

A normal type of business organisation, and one which can be followed in all its details, cannot be derived from an examination of a single business. In fact, it is impossible to lay down a business organisation suitable for all cases; and, in order to obtain a good practical and well considered scheme, it is necessary to keep fully in mind the peculiarities of the trade, the nature of the business, the local conditions, the special wishes of the directors, the existing customs, the extent of the business, and many other things.

**GENERAL ORGANISATION OF WHOLESALE WAREHOUSE.**—The organisation of the wholesale warehouse can, therefore, only be dealt with in general terms. From that point of view, the business can be regarded as being organised into three main departments—

- (1) The Buying Department.
- (2) The Selling Department.
- (3) The General Administrative Department.

**THE BUYING DEPARTMENT.**—The nature of the business will probably be such that it deals in many quite different varieties of goods and, therefore, there will be subdivisions according to the different classes of goods dealt in, and each of these will be called a department. Each department is usually controlled by a manager, who is known as the *Buyer*. The departmental manager is primarily responsible for the buying of his department, so that the business is grouped as a whole; the purchase of goods of a particular description is thus effected by a responsible person, and in this manner a stock is provided from which customers can select the goods they want to buy.

**QUALITIES OF A GOOD BUYER.**—The chief duties of the buyer are to get into touch with the best sources of supply, to find out the conditions and limitations in connection with the goods that can be supplied, to place orders, and to keep in touch with new ideas. It is clear that the good buyer must be decidedly



unimpressible to others; he must be a man with his own opinions, and capable of holding them sufficiently to prevent him from being talked over by others who may be interested in so doing.

**AUTHORITY OF THE BUYER.**—The departmental buyer may be granted authority to buy from the source he thinks best; or the General Manager, who is responsible for the business as a whole may sanction his suggestions before they can be acted upon. As to which of these two plans is the better will depend upon the personality of the departmental manager and the General Manager. Given two persons in responsible positions—one subordinate to the other—the problem is to find the best arrangement to promote efficiency in the best sense of the term. Unless the men work together well and both are satisfied with the terms under which they work, efficiency cannot be obtained.

If the general manager knows a great deal more about the business than the departmental manager, it seems reasonable that the general manager should really control the departmental manager's actions. In that case, the departmental manager may be little more than an assistant manager, so long as the general manager possesses the knowledge and experience to enable him to fill the position. If he is not possessed of the necessary knowledge, time, and energy, it is very much better that he should not attempt the work. But if the management of the department is in the hands of the buyer, then, on the whole, the less he is interfered with from above, the better the results will be. This means that he is given a free hand within certain specified limits, and is judged according to the results he is able to produce.

As a rule, the best results will be achieved by giving the departmental manager or buyer a free hand to purchase where he likes, but that may be subject to modification. For example, whenever he opens a new account, he may be required to report the fact to the general manager, with a short statement of his reasons for opening such an account. The mere fact that he has to do this is a reminder that, other things being equal, one does not require to open new accounts merely for the sake of doing so. A business house is likely to get more consideration from its sources of supply if the orders it gives are sufficiently large. It is therefore important to remember there is a limit to the splitting up of orders given.



**CHIEF FACTORS IN BUYING.**—The main factors which should influence the buyer in placing his orders are—

- (1) The nature, quality, and description of the goods.
- (2) Whether they are the goods he wants.
- (3) Whether the prices are suitable.
- (4) Whether the time of delivery is suitable.
- (5) Whether the delivery will be in accordance with what was ordered.

It is largely owing to the great inconvenience caused by not getting what was expected when delivery comes, that, as a rule, it is better to buy from houses that one does know rather than from strangers.

Good business houses are always striving to build up a good reputation; and one of the most important items in that reputation will be not merely that the goods come to hand at the time they were promised, but that when they come to hand they are of a saleable description in every sense of the term.

Supposing an order has been given for chinaware and, when it is delivered, about 30 per cent of the goods are broken. It is not merely a matter of seeing that the manufacturers give credit for what is broken, but there is the trouble of sorting out the defective goods and the use of additional warehouse space involved. Under proper conditions, there would have been no need to look through the goods, but they could have been sent direct to the customers if ordered. Thus, there is a great saving if the goods are received in a merchantable condition.

**POLICY OF THE BUYER.**—The buyer may be said to have two business policies to choose from in deciding what commodities he will deal in. He may—

- (1) Get into touch with the customers and supply them with what they want; or
- (2) Find the most saleable articles and then try to push them on to the customers.

When the customers of the wholesale warehouse are themselves expert buyers, the probability is that they know what they want before they make out their orders, and will not depart from their original intention. Occasionally, however, they may be induced to place an order for something they have not seen before it is shown to them. The most prudent policy of the wholesale buyer



is to find out what the customers want, and then consider the buying from that point of view instead of always launching out on new lines. On the other hand, if the customers are the general public, as in the case of the retail trade, the question is not so much as to whether they want the goods or not, as to whether they can be persuaded that they want them. Here the chances of selling will be increased if the most saleable kinds of articles are considered beforehand and then stocked heavily without waiting for orders.

Speaking broadly and subject to a considerable margin for exceptions, it may be said that in the wholesale trade less initiative is required on the part of the buyer than in the case of the retail business. This is, of course, a broad generalisation and subject to considerable modification in practice.

**THE SELLING DEPARTMENT.**—The next division of activity in the wholesale warehouse is what is known as the Selling Department. The object of this department is to find purchasers for the goods that are on sale in the warehouse, and to get orders for goods which are capable of being executed. The possibilities of organisation in connection with the Selling Department are as yet but little understood in England. This is shown in the fact that very commonly there is no recognised division between the buying and selling departments. Very often the skilled buyer is also made responsible for the selling of the goods. In one sense, this is convenient, since there is no divided responsibility; and if the buyer has to find purchasers for the goods he has bought, he cannot shift the responsibility of the failure for so doing on to someone else. But if it is recognised that the selling of goods is not the same thing as buying them, and that there is scope for the exercise of different qualities in successful salesmanship as compared with successful buying, the probability is that these qualities are not likely to be found to their fullest extent in the same individual. Hence, where the business is sufficiently large, buying and selling should be kept as distinct departments, so long as they can be so co-ordinated as to work together harmoniously.

**QUALITIES OF A GOOD SALESMAN.**—If a salesman is to be a success, he must be an optimist. He must be able to see the good points of the goods he has to sell and, further, he must exercise some sort of influence on customers, so that, if



possible, he can infuse his optimism into them and get them to buy.

In these days of competition, a business house that makes no attempt to get orders out of customers is likely to be left behind. If the trader is to effect an increasing turnover, he must use every effort to find new methods of reaching his customers.

Of course, the art of salesmanship consists of a great deal more than simply being on the spot ready to attend to customers when they come. But even here there is some scope for the peculiar qualities of the salesman. It is clearly important to get the customer in the right vein to appreciate what the salesman has to say. The customer is human and has to be instructed. This may require great tact, because he may have to be instructed (without giving offence) as to what he really wants or ought to want—a point about which customers are very sensitive. They think they know their requirements, when perhaps they do not.

In making his purchases, the buyer can be as rude as he likes, and still his orders will usually be accepted. This is not so with the salesman. He must always be polite to his customers if he is to induce them to make additional purchases to what they had first intended. It is the art of salesmanship which will induce the right frame of mind on the part of the customer. This applies particularly in the retail trade, where the salesman comes into direct contact with the general public and also, in a lesser degree, to the wholesale salesman whose customers are skilled professional buyers. It may not always mean that the customers are persuaded to buy goods that they do not want, but they may be led to place orders that they intended to place elsewhere.

**WHOLESALE METHODS OF DISTRIBUTION.**—It is one thing to provide a salesman competent to handle customers, but the wholesale house which desires to increase its business substantially must look a little farther afield for new trade—either trade with new customers, or trade extending over a wider area of goods, or both. Examples of both these methods can be seen in operation at the present day. Progressive business houses increase their premises to cope with increased business, and this, in turn, brings an increase in the number of their regular customers engaged in either the wholesale or retail trade. Along with this activity, business houses are constantly adding new departments or



embarking on new kinds of trade, which they carry on side by side with their existing business. In this way, they are able to cater for other wants of existing customers, which hitherto had to be fulfilled by other persons.

The expansion in the direction of new activities and new departments seems to meet with greater promise of success in the case of wholesale houses with a good *clientèle*. But it is no good starting trade in new lines of goods of which one has but little knowledge, for, to be dealt with effectively, each kind of goods requires its own kind of knowledge. To some considerable extent, the want of knowledge of details may be supplied by engaging really competent buyers of the new departments. The buyer should have all this detailed and specialised knowledge even more than the general manager, who should ensure that this is the case.

When it is a question of trying to acquire new customers, there are, broadly speaking, four ways of proceeding—

(1) **To Rely upon Reputation and the Recommendation of Existing Customers.** This is a slow process at the best. In the retail, it is a usual practice, but is not of much use in the wholesale trade. The reason for this is that the customers of a wholesale trader do not see very much of each other. Their opportunities of communicating with each other are not great, in addition to the fact that they are, in the nature of things, competitors.

(2) **To Employ Travelling Salesmen.** It is the duty of travelling salesmen to call upon business houses, to show samples of goods to prospective customers, and to do their best to get trial orders. One trial order having been obtained, it may be usual for the business to rely upon the value of the goods and upon their general reputation to get repeat orders from it. This does not mean that when once the trial order has been given, the traveller has not to interview the customer again; on the contrary, he must constantly nurse the customer.

In the wholesale trade, there is great scope for the development of trade by means of travelling salesmen. This is particularly the case where the probable customers are residing at some distance from the firm's headquarters (e.g. the provincial trade in regard to a London house).

(3) **To Appoint Agents.** The appointment of agents by the



wholesale firm serves exactly the same purpose as that of the travelling salesmen, except that the agent, as a rule, is resident in a centre where he is already fairly well known, and therefore has a better footing than could be obtained by itinerant travellers.

(4) **To Use the Medium of Advertising.** In regard to the wholesale trade, advertising is most marked in the case of branded goods. It is of little use for the wholesale house to advertise in the hope that retailers will notice the advertisements, and will instruct their buyers to call and see whether the house is worth patronising.

If a wholesale house sells goods bearing a specific name, it may with advantage advertise, in order to appeal to the general public. If the advertisement is successful, it will create a demand by the general public which will cause retailers to place orders with the wholesale house. In so far as the articles are of such a description that the orders must come to the advertisers, it may be a good thing; but if the orders may go to substitutes, the advertisement may prove wasteful.

**SELLING—THE LINK BETWEEN BUYING AND FINANCE.**—The salesmen, whose business it is to supply the requirements of customers, have opportunities of finding out what the customers really want, which the Buying Department, as such, does not possess. Customers will state their wants, and it is an essential factor of the sound organisation of a wholesale house that any want which cannot be filled out of stock should be communicated to the Buying Department with a view to seeing whether it ought to be stocked. This is important, because the customers of the wholesale house are themselves professional buyers, who presumably know their business. If they want a particular class of goods, the presumption is that there must be a demand for it. It is therefore worth while considering whether to supply it.

In the same way, the Selling Department must keep in touch with the Finance Department, or chaos will soon result. Just as no business house can afford to buy without considering how much capital may be locked up in stock, so no business house can afford to sell on credit without considering how much capital may be locked up in book debts. This is a question of finance and not of selling.

Salesmen, being temperamentally optimistic, are not to be



trusted in deciding as to whom credit shall be given and upon what terms. The Finance Department should look after this work without causing any friction. The linking up of one department with another may easily cause friction if it is not done with considerable ability and with the exercise of reason.

**GENERAL ADMINISTRATIVE DEPARTMENT.**—It has been seen that in connection with both buying and selling, a considerable amount of expert knowledge is required with regard to the particular kinds of commodities that are being dealt in ; whereas what constitutes ability in the direction of finance or administration is really very much the same under all conditions, whatever the precise class of goods may be. A capable administrator of one kind of business should, with comparatively little expenditure of time, make himself capable of managing another business.

**Financial Administration.** The first point to be considered is that of capital, since any kind of business house, if it is to be financed on sound lines, must have a certain amount of capital adventured in the business. What is meant by capital is a definite fund represented, in the first instance, by money or by some form of property capable of being used with advantage in connection with the business. It must, therefore, consist either directly or indirectly, of money permanently adventured in that undertaking, and must not be capable of being withdrawn at the whim of anybody desirous of using it for other purposes. When a wholesale house is organised on the lines of a limited liability company, it is natural that it should have a capital of that description. In fact, the company law of this country fits in with the requirements of the position in that it expressly provides that capital subscribed by the members of the company shall not, except in very special circumstances, be returned to them during the time the company is in operation as a going concern.

Whatever the nature of the business, any serious drain upon its capital, or repayment of capital to members, must leave the undertaking in a more difficult position to carry on the undertaking than before. It must, therefore, be assumed that there is not merely a fund for the purpose of financing the business, enabling it, when necessary, to pay its debts without being forced to a realisation of its assets, but also a fund for any unforeseen contingencies. Sometimes in connection with a wholesale business.



there may be one or two seasons of the year when standing expenses exceed the normal profits. It is necessary to have capital to tide over a period of that kind, and still more to tide over quiet times which do not recur with regularity.

Capital is also required for the purpose of providing equipment, after the payment for which there should be left a sufficient margin as *working capital* to finance the concern. Working capital is required, because in the normal course of events, money is spent before it comes back with a profit in an augmented form. Money must be spent before one receives, although there are some exceptions to this rule. Some businesses sell only for cash, and therefore they receive payment for the goods they sell before they themselves have paid for them. Such businesses, however, would not be included under the heading of wholesale concerns.

The probability is that the wholesale house will give a longer period of credit to its customers than it receives from its supplying house. Here, again, there are exceptions dependent upon particular trades and different classes of customers. If the customers of the wholesale warehouse are customers carrying on a cash trade, the probability is that they will be anxious to get close prices on what are known as *prompt terms*, and in those circumstances it is very likely that the wholesaler will receive payment before he himself is obliged to pay for the goods he has bought.

The standing expenses of a wholesale house are, on the average, about 10 per cent, and its profit is usually from 14 to 17 per cent on the sales. This is, of course, prior to taking into account any kind of contingencies which will arise in the way of bad debts, special losses due to changes of fashion, etc. A wholesale business which can, year after year, realise a net profit of 10 per cent on the capital employed is usually regarded as being very satisfactorily managed. The amount of capital required to carry on the business depends a great deal upon the length of credit given. This will be, roughly speaking, about one-fourth of the amount of the sales.

**Debentures.** It is an open question whether there is absolute safety in connection with investment in a wholesale warehouse. It is, therefore, customary to issue capital in the form of debentures. In the strict sense of the term, these are not capital at all, but simply money lent at a fixed rate of interest and repayable on fixed



dates. The majority of persons who invest their money in debentures consider that the debentures are secured by a mortgage on the assets of the business, although this is not always the case. When they are secured and the assets are of sufficient value, the security is good; and if there is a default in the payment of interest, the debenture holders can put the law into motion and compel the assets to be sold. Their claim ranks before that of creditors, who are not similarly secured. The disadvantage of industrial debentures, as they are called on the Stock Exchange, is that the undertaking issuing them has naturally to have a considerable amount of capital sunk in business premises and equipment.

### TEST PAPER LXII

1. What considerations must be borne in mind in drawing up a scheme of organisation?

2. Into what three main departments can the organisation of the wholesale warehouse be divided?

3. What are the qualities of a *good buyer*?

4. What authority should be conferred upon the buyer of a wholesale warehouse?

5. Enumerate the main factors which should influence the wholesale buyer in placing his orders.

6. With what two business policies is the wholesale buyer confronted when deciding what commodities he will deal in?

7. Under what circumstances should the selling department of a wholesale warehouse be separated from the buying departments?

8. Compare the qualities of a good salesman with those of a skilled buyer.

9. What four methods are adopted by the wholesale warehouse in order to acquire new customers?

10. Show how selling acts as the link between the buying and financial departments.

11. Mention some of the points to be considered in financing a wholesale warehouse.

12. Compare the methods of the wholesale trader and of the retail trader in the purchasing and selling of commodities.

13. State the functions of a wholesale warehouse and indicate a suitable scheme of organisation that will adequately control these functions.

14. Wholesale warehouses have been likened to banks and warehousemen to bankers. Develop this analogy.

15. Explain the important differences in the organisation of a wholesale warehouse as compared with that of an ordinary retail shop.

16. If all wholesale business were abolished and goods were sent directly to the retailer from the producer, in what ways would the shopping public probably be affected?



## CHAPTER LXIII

### THE MEANING AND CALCULATION OF TURNOVER

THE endeavour to obtain the maximum return to his efforts leads the merchant into the avenue of economy (i.e. to effect his part in the exchange of goods with the least possible expenditure). His private interest is the realisation of a large profit, which consists in the difference between his buying and selling prices, so that the principle of cheap buying and dear selling evolves quite naturally. The wholesale trader endeavours to purchase his goods as cheaply as possible from the manufacturer or producer, so that, in practice, the art of trade consists in the application of all those means and methods to attain that end. For this purpose, the merchant must take a clear view of the whole market, such as the supply of goods in the hands of the manufacturers or producers, the visible and invisible stocks, the conditions of production with their attendant drawbacks, and a most careful study of the fluctuations of trade as far as his specialised commodity is concerned. In doing this, he certainly acts in conformity with economic principles.

**LIMITATIONS TO CHEAP BUYING.**—There are, of course, limits to cheap buying. If the manufacturer has the choice of several buyers in the disposal of his goods, he will cut off his business relations from those who seek to take advantage of him. Again, every merchant who intends to make a permanent living out of trade, and who desires to secure reliable sources of supply, must aim at giving fair treatment to those who supply him. The fact must not be overlooked that it is possible for the manufacturers to combine for the purpose of selling should the merchant refrain from offering a fair market price. The single business, therefore, digs its own grave if it is impelled solely by selfish motives when effecting its purchases. Buying cheaply has, therefore, its limits, which are determined by competition and the considerations of a permanent and secure business connection.

From a business point of view, it is unwise for a trader—whether wholesale or retail—to change his dealers whenever a lower quotation is offered to him. Naturally, he will compare the various



offers made to him, with regard to their quality and price, with those at present supplied to him ; but, at the same time, he must also examine whether the new quotation is nothing more than a bait, and whether the new firm would be as capable of serving him as the present, and whether his special wishes and requests respecting the time of delivery and quality could be executed. From a consideration of these important factors in buying and selling, it must be concluded that the cheapest quotation is not always the best.

**LIMITATIONS TO DEAR SELLING.**—The same applies to the principle of selling in the dearest market. However natural it may appear that a merchant, in his endeavour to increase his profit, must strive to fix his selling price as high as possible, the wise merchant must, above all, be moderate in the settlement of his prices. Apart from the fact that he must ever take into consideration the question of competition in fixing his selling prices, the merchant can acquire a permanent *clientèle* only by meeting his customers in a reasonable manner, especially since business success does not, as a rule, depend on a single transaction, but on a permanent connection and a regular *clientèle*, which the merchant can secure only by working at a small profit. However paradoxical it may seem, the correct principle of business practice is to sell as cheaply as possible, assuming naturally that the limits of the selling price have been fixed by a careful analysis of the cost. The analysis of the cost must lead the merchant to observe that the difference between the buying and selling prices, or the *profit* on a single transaction, forms but one of the three factors on which together the success of an undertaking depends. The other two factors are the *magnitude* and the *rapidity* of the turnover.

An example will explain the mutual dependence of these three factors—

Let us suppose three competing merchants—A, B, and C—are dealing in wheat.

A buys 100 qrs. wheat at 15s. qr. and sells them at 16s. ; he turns over this quantity every month : therefore his yearly profit amounts to 1,200s.

B has a turnover each month of 400 qrs., which he purchases at 15s. 2d. and sells at 15s. 8d., thus gaining 6d. on each quarter, and his yearly profit amounts to 2,400s.



C buys 400 qrs. at 15s. 4d. and sells them at 15s. 6d., but can effect a turnover of over 400 qrs. per week. Although his profit on each quarter of wheat is only 2d., he makes a yearly profit of 3,466s. 8d.

The first merchant (A) acts according to the principle of buying in the cheapest and selling in the dearest market ; whilst B acts on the principle that, in spite of a lower selling price, a bigger profit can be obtained with a large turnover than with a big profit and a small turnover. C recognises the basic principle—the effect of a large turnover—but to this he adds a new principle in that he turns over the same quantity not monthly, but weekly, and thus obtains the highest total profit, although he buys in the dearest and sells in the cheapest market. His guiding business principle is to effect a speedy turnover.

From this example, further conclusions may be drawn. A pays to the producer 15s., B 15s. 2d., and C 15s. 4d. per quarter.

In effecting his purchase, C will defeat his competitors A and B, or at least will render less favourable their conditions of purchase. Again, since C also comes in touch with the consumers with the lowest selling price of 15s. 6d., whereas B demands 15s. 8d. and A 16s. per quarter, he will immediately capture the best customers and thus relegate the other sellers into the background. To this is added the greater efficiency, regularity, and better organisation which C possesses over A and B, which will benefit the parties which are brought together by him, viz. the producer and the customer. The more efficient the business organisation, the more effectively does trade play its part in the national economy. Moreover, from the example above given, it will be seen that the individual's desire to make profit leads automatically to higher economic principles ; and that the well-known commercial maxim of buying in the cheapest and selling in the dearest market is by no means the determining one, but must subordinate itself to other principles, and especially to that of effecting a speedy turnover.

A simple arithmetical example has shown that the effecting of a large turnover is of the greatest importance to trade.

Attention will now be drawn to some general points which must be kept in mind in the endeavour to achieve this end.

**INFLUENCE OF A LARGE TURNOVER ON TRADE.**—The aim of



every merchant to enlarge his turnover is subject to limitations. Both the quantity of the products and the extent of human needs are limited, so that it is impossible for every merchant to increase at will his turnover. As in the past, so in the future: there will be competitive undertakings on a small, medium and a large scale. The small business has a hard struggle, and utilises a thousand different ways and means of retaining its existence alongside and amongst the large undertakings. Its existence is based chiefly on the personal character of the owners, and the power to adapt themselves to peculiar circumstances and, especially, in the willingness to accept a more moderate return. But the gaps and imperfections of large-scale enterprise not only admit of a large number of small businesses, but open the way to their success. The proof of this is to be seen in the fact that within the last twenty years, in nearly every country, and in spite of large stores and co-operative societies, the number of small retail businesses has increased at a more rapid rate, relatively, than the population.

**FACTORS IN EFFECTING A LARGE TURNOVER.**—The scope for developing and the possibility of establishing a large-scale undertaking, and thus effecting a large turnover, is always restricted to a limited number of firms. One of the most salient factors is to be found in the extension of the circle of customers, and the effecting of a large turnover centres chiefly around the struggle for customers.

Taking a broad survey of the *clientèle* for which businesses are called into existence, it must be borne in mind that this is no stationary factor, and that it depends not only on the number of people whose needs must be satisfied, but also on the varying extensity and intensity of their needs.

The variation in the intensity of human needs affords in itself an opportunity to the merchant for the extension of his business and for the enlargement of his turnover. The conflict for the *clientèle* manifests itself in a definite area, so that to effect a large turnover it is necessary to capture a large circle of customers. Among the most important characteristics of modern trade is this struggle for customers, which often assumes some of the keenest and most repugnant forms of commercial warfare.

The struggle to extend one's business connection, or the endeavour on the part of each firm to increase its turnover, may finally prove



disastrous to all interested in the particular trade, so that the concerns are eliminated, whilst the better managed and more efficient are worked at a loss. Here, then, is the starting-point for cartels and syndicates, which will be discussed in a later chapter. Suffice it here to point out a tendency which is closely connected with the attempts to augment the turnover by increasing the number of customers. This tendency consists of two forms of restricted competition : one an agreement on the part of competing businesses to safeguard themselves against the customers (i.e. an association of sellers) ; the other, an agreement to allot definite trading spheres to different merchants and manufacturers.

Experience has shown that neither one nor the other of these agreements lasts for long. The varying degrees of efficiency, and the desire on the part of each business for further expansion, always precipitates a breach of contract and leads to its dissolution. It is clear that these tendencies towards dissolution are mainly to be found among the more powerful combinations, which, in their thirst for enterprise, become dissatisfied with the permanent restrictions of the cartels and syndicates. Generally speaking, however, the break up of these combinations is beneficial to trade, for society has no interest in the maintenance of inefficient concerns by artificial means. It is, however, beneficial to eliminate the smaller concerns or to restrict their sphere of operations, so that the more efficient firms, which can exercise the economic principle of trade, may survive. Hence it may be concluded that a large turnover depends principally on a larger sphere of customers, which can be gained only by those businesses which are efficiently organised.

Nevertheless, the endeavour to extend the sphere of trade and its customers, in order to increase the turnover, may be unprofitable to the single business and disastrous from the economic point of view. This is especially the case with regard to mercantile concerns, in which expansion is accomplished with a relatively high rate of selling expenses ; or where the sale of the increased purchases becomes impossible, so that they have to be cleared at a loss, or at such a price as to be damaging to the whole market.

A sound and profitable increase of turnover cannot be forced, but depends upon the possession of a greater business efficiency over one's competitors, although, in some cases, it may be due

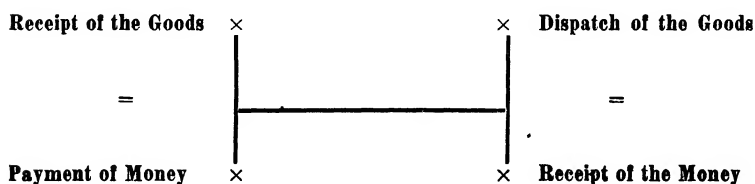


to the command over capital. The latter, however, are the exceptions rather than the rule, so that, apart from these, superiority is to be sought for in the normal factors, such as in a more complete organisation of business, whether in regard to purchasing, warehousing, selling, working expenses, quality, cheaper prices, goodwill, in the better adaptation to the requirements of the customers, or in greater activity and initiative.

**INFLUENCE OF THE PERIOD OF TURNOVER.**—In addition to the two factors—the difference between the purchase and selling prices (i.e. profit) and the magnitude of the turnover—there comes a third: the period of the turnover or the necessity of effecting the turnover as speedily as possible.

In order to explain the relationship existing between the time and the magnitude of the turnover in reference to the practice of commerce, it is necessary to examine the basis of the circulation of business capital.

If the goods are bought with cash on the spot and again sold for cash, the whole circulation of the turnover is limited by two points of time. The starting-point for the period of the turnover is the day on which the goods were received, and with this coincides the day of payment. The termination of the period of turnover, or the circulation of the goods, is the selling day when the goods are dispatched, on which, according to the above illustration, payment is received for the goods.

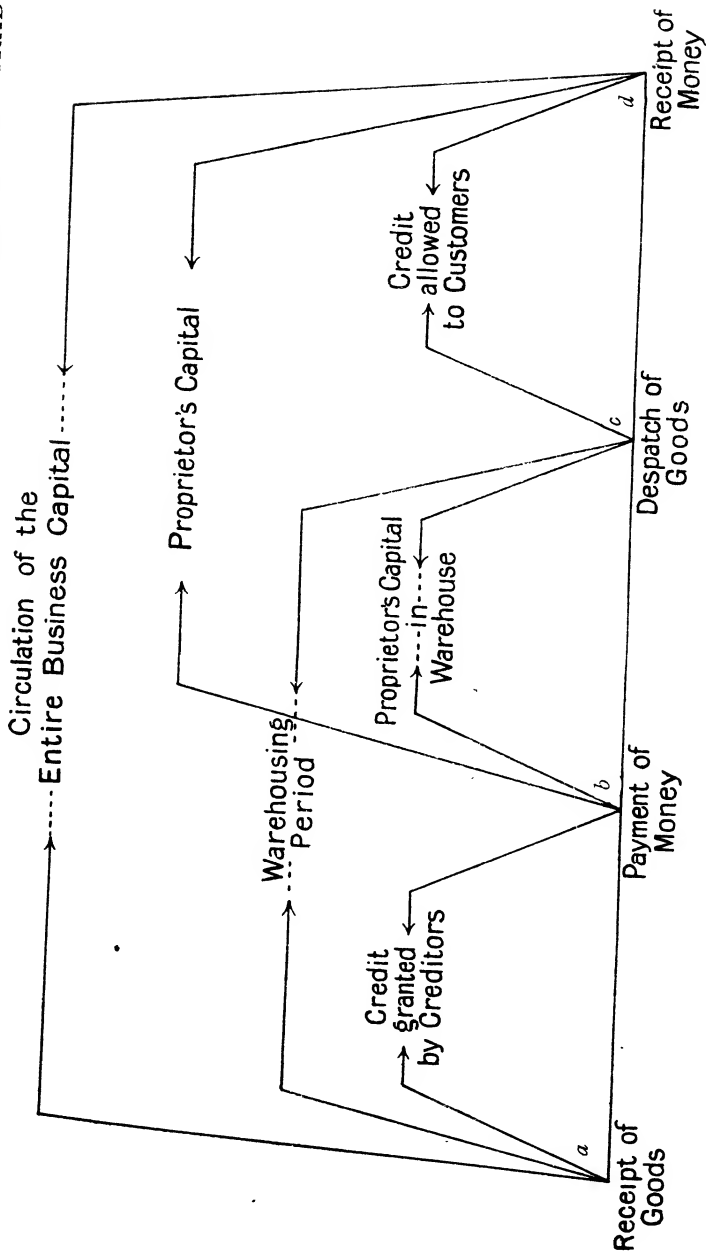


If, however, the purchase and the sale are not effected in one and the same place, but at a distance and on credit, there result four points of time, which as a rule, come in the following order—

**Receipt of Goods — Payment of Money — Sale of Goods — Receipt of Money.**



DIAGRAM ILLUSTRATING THE INFLUENCE OF THE PERIOD OF TURNOVER ON TRADE





Various modifications, however, are possible. The time for the payment of money may be effected after the sale of the goods ; indeed, even after the time of receiving the money.

**DIFFERENT MEANINGS OF TURNOVER.**—From the diagram on page 563, the following results may be drawn—

I:  $a-c$  is the period of time during which the goods remain in the warehouse, or, when purchased at a distance, transit and warehousing period are combined. In the diagram these are marked "Warehousing Period."

II:  $a-b$  indicates the period of credit granted by the creditor, during which the trader is indebted for the purchase value of the goods in stock.

III:  $b-c$  is the period of time during which the stock of goods purchased by the trader's own capital remains in the warehouse.

IV:  $c-d$  is the period of credit allowed by the trader to his customers, during which period this portion of his capital remains in the hands of his debtors ; it is marked "Period of Credit granted to the Customers."

V:  $b-d$  is the period of time between the payment and the receipt of the money, and this indicates the duration of the circulation of the working capital engaged in this business ; for a time it consists of stocks as in  $b-c$ , and also assumes the form of amounts owing by debtors as in  $c-d$ . The entire distance from  $b-d$  is the period of the turnover of the owner's capital.

VI:  $a-d$  indicates the period of time for the circulation of the whole business capital (i.e. of the outside capital in the form of goods sent to the trader on credit), and his own capital = the period of turnover of the entire business capital.

From this it may be concluded that "turnover" has the following different meanings—

- (1) Period of Turnover for the Entire Working Capital ( $a-d$ ).
- (2) Period of Turnover for the Owner's Capital ( $b-d$ ).
- (3) Period of Turnover for the Goods in Stock ( $a-c$ ).

**CALCULATION OF THE WAREHOUSING PERIOD.**—Since the trading profit is realised from a legal and accountancy point of view at the time the goods are sold and handed over to the customer, the termination of the period of warehousing is, of course, at  $c$ , and not at  $d$ , as is often erroneously presumed. Moreover, as the



period of credit granted by the supplier of the goods is based on circumstances which have nothing to do with the period of warehousing, *a*, and not *b*, is the starting-point of the period of turnover. The period of warehousing is regarded as the time from the receipt of goods (when purchased at a distance from the date of the invoice) up to the dispatch of the goods.

At first, it is necessary to inquire how the period of warehousing is determined in a commercial concern. For this, there are two methods: the direct calculation and the calculation of the average.

The *direct calculation* of the period of warehousing, and the only reliable one, consists in tabulating the dates of receipt and of dispatch of each individual transaction, and thus compiling statistically the period of time. This method is easily applied in the wholesale trade, when similar quantities of goods are dispatched in the same packings as those in which they were received, as in the case of wagon-loads and shiploads of coal, wheat, sugar, or with machines, pianos, animals, etc.

In the retail trade, also, the direct calculation of the period of warehousing may be adopted, especially when the articles enter and leave in the same form, as in the case of furniture, clothing, watches, jewellery, etc. Here the merchant will insert on the labels, which are attached to each article, the date of the receipt, and at the sale the date of the dispatch of the goods, in order to be able to arrange them in statistical order. With the aid of these details and the repeated inspection of the stock-room, the merchant will be enabled to discover immediately whether there are any goods which have been in stock too long, and are now out of date and unsaleable, so that he is in a position to make his arrangements accordingly.

The determination of the period of warehousing is much more difficult when the goods are subdivided, re-arranged, or packed differently; or if the sale takes place in small quantities, according to measure or weight; or if the quantities for sale become so numerous and small, that it is impossible to record them statistically, as in the case of wines, drapery, hosiery, toys, etc.

In all these cases, the *Indirect Method* is used. The determination of this average is to be seen from the example given on the next page.



	£
Value of Stock at the beginning of the year . . .	88,000
Value of Purchases during the year . . .	224,500
	<hr/>
Total of Goods received . . .	312,500
Less Stock at the end of the year (at Cost Price). . .	95,500
	<hr/>
	217,000

The cost price of the goods sold during the whole of the year, and calculated as above, is compared with that of the average value of the stock. Should there be no details concerning the interim stocktaking, the average value may be taken from the last two periods of stocktaking. In the above example, this average =  $(88,000 + 95,500) \div 2 = \text{£}91,750$ .

It is possible that this calculated value of the average stock does not agree with their actual value, especially when the stock during the year changes considerably. Particularly is this the case with seasonal trades, in which the stocktaking occurs during the slack period when there is little stock. In such cases, recourse must be had to interim stocktaking. From the proportion of the year's turnover in relation to the average stock is derived the average period of warehousing, which, in the above example, is as follows—

$$217,000 : 91,750 :: 365 : x, \text{ where } x = 154.3.$$

Thus, the average period of warehousing is 154 days, so that the average stock is turned over 2.3 times during the year. Each period of warehousing is charged interest at the rate of 5 per cent per annum, but the amount for 154 days is only 2.11 per cent interest.

It must not be forgotten, however, that the warehousing period determined in this way is an average ; and as these average figures are not exact, a method must be sought whereby this average may be completed, especially where trade is done in several varieties of goods. Here a classification is required giving the groups of goods from which, in each case, the yearly turnover (at cost price) and the average stock have to be calculated.

The period of warehousing and the method of its calculation having been defined, the next step is to examine the effect of the



warehousing period on the conduct of business and the conditions upon which this period depends.

**STATISTICS.**—These are important to the manager of a wholesale trading concern because they enable a comparison to be drawn between past and present results, with the two-fold object of increasing output or reducing expenditure so as to increase profits. All items of expenditure can be classified and readily compared with the relative amounts of the previous period, thus bringing under review excessive expenditure which would not otherwise be so apparent. The output and profits can, however, also be taken into consideration.

### TEST PAPER LXIII

1. Mention some limitations to cheap buying.  
2. "The profit on a single transaction forms but one of the three factors on which together the success of an undertaking depends." Examine carefully this statement and name the other two factors.

3. Criticise the well-known commercial maxim of "Buying in the cheapest and selling in the dearest market."

4. Enumerate some of the factors which enable the wholesale merchant to effect a large turnover.

5. Explain how the period of the turnover is calculated when goods are bought for cash and sold for cash.

6. Copy the diagram on page 791 and explain clearly its meaning.

7. Explain the different meanings attached to the term "Turnover."

8. Describe the methods adopted for the calculation of the warehousing period.

9. (a) What connection exists between the rapidity of turnover and a trader's profits?

(b) A retailer had £2,000 invested in his business. His turnover for the year was £5,000, and his gross profit 10 per cent on the turnover. If his expenses amounted to £250, what was the rate of his net profit on turnover and on capital?

10. A trader is asked to sell at 2s. 6d. an article, A, which is sold to him for 2s. Another manufacturer offers him a slightly inferior article, B, of the same kind for 1s. 8d. to sell also at 2s. 6d. Find his gross profit and his percentage of gross profit on turnover in the three following cases—

(a) He buys 12 doz. of A and 8 doz. of B, and sells them all in two months.

(b) He buys 18 doz. of A and sells all in two months.

(c) He buys 12 doz. of B and sells all in two months.

Which of these three courses is the most desirable to pursue, and why?

11. A merchant's accounts reveal the following position for two successive years—

1st Year			2nd Year		
	£			£	
Sales	20,000		Sales	25,500	
Sales Returns	1,000		Sales Returns	1,500	
Gross Profit	8,000		Gross Profit	9,500	
Expenses	5,000		Expenses	6,000	

Find (a) the percentage of gross profit to turnover in each of the two years;

(b) the percentage of net profit to turnover in each of the two years. What useful information is provided by these calculations?



## CHAPTER LXIV

### PROFITS IN RELATION TO TURNOVER AND WORKING EXPENSES

A TRADER who turns over his stock only once during the whole year must fix his profit fifteen times as high as that of his competitor who turns over his goods in twenty-four days, if he desires to earn the same total profit. Moreover, his competitor has the advantage over him in several ways. The long warehousing of the goods entails labour, interest on capital, and warehousing expenses. It is also possible that the goods may be depreciated in consequence of a long period of warehousing.

**THE DIRECT EXPENSES OF WAREHOUSING.**—As may be seen from the price list of any firm of warehousemen, the expense of warehousing grows in proportion to the length of the warehousing period. The same, of course, applies if the trader stores the goods in his own warehouse. Hence, in the calculation of the warehousing expenses, account must be taken of the rent, depreciation, and maintenance of the warehouse buildings, and these expenses have to be spread over the various goods in proportion to the time and space occupied by them. Therefore, the quicker the goods pass through the warehouse, the smaller is their share in the warehousing expenses. Many concerns, and especially those engaged in the intermediary trade, try to avoid altogether the expense of warehousing the goods. For instance, commission agents engaged in the import and export trades often sell goods afloat even before the arrival of the vessel. Again, they may only undertake to consign goods abroad when they have found a customer for them. In fact, it is the rule in export trade for the trader to have no warehouse at all. In certain branches of the wholesale trade, a definite period is allowed for the acceptance of the goods, so that the exporter has an opportunity of selling these goods within that period without the necessity of warehousing them. Hence, he saves not only the warehousing expenses, but also the carriage inwards and outwards.

On the other hand, there are many undertakings which are compelled to maintain large warehouses; and especially in those wholesale and retail trades which desire to offer their customers,



not only a large selection of goods, but also to keep large quantities for sale. This is also the case with goods which cannot be turned over within a short period, such as fancy goods, watches, etc. Very often, also, the period of warehousing is prolonged when it has an influence on the appreciation of the quality, as in the case of wines, spirits, pictures, and stamps. Here the warehousing expenses are amply compensated through the increase in value of the goods. Indeed, in such cases the stocks may be considered as a lucrative investment of capital.

**WAREHOUSING, LABOUR, AND OTHER EXPENSES.**—Almost all goods require, during their period of warehousing, a careful treatment against internal or external decay. Some have to be protected against dampness; others against dryness, heat, cold, light, wind, and weather; some are subject to depreciation, others to leakage and evaporation. Some, such as woollens, corn, and flour, are endangered by insects; whilst others are injured by rust and loss of colour. All goods warehoused must, without exception, be insured against fire and theft.

**Depreciation.** Only in the case of a few goods is their quality or value increased through warehousing. As a rule, depreciation sets in, and this is all the greater the longer the period of warehousing; most noticeable is this in the case of fashionable goods. Fortunately, almost every fashion finds its way from the capital into the small towns, then into the villages and into the remotest parts of the world, so that the warehouser is able to send into the provinces stocks which happen to be unfashionable in the capital. The necessity here arises, however, of clearing the stock at the right price. To-day, not only are clothes slaves to fashion and its changes, but nearly all commodities, such as watches, fancy goods, furniture, china, pictures, books, and a thousand other articles. Therefore, the risk of the depreciation of goods in the warehouse is spread over a large number of commodities, and it is worth while to point out the means at the command of a mercantile concern to provide for this depreciation.

In the first place, an amount can be added to the cost price for the depreciation of the unsaleable stock. For this reason, the so-called articles of novelty are the dearest. Another means is the clearance of the warehouse at the end of the season by the holding of special sales.



One of the greatest mistakes in business is the failure on the part of the proprietor or manager to clear the old stock at the right time and the unwillingness to reduce the prices in the false hope of finally obtaining the old prices. If he has calculated correctly and has included in his selling price an amount for the depreciation of the unsaleable stock, then the reduction of price and the allowance at sales is only an apparent loss. Although the merchant may correctly estimate the warehousing expenses and the depreciation, he will risk much more if he keeps old stocks for long periods of time. One of the requirements of a satisfactory business system, therefore, is the periodical checking of the stock and the clearance of ante-quoted goods. This applies not only to retailers, but is also applicable to the wholesale trade.

The quicker the turnover, the smaller is the capital required for an equally large turnover. That concern which turns over slowly its capital will require more than its competitor which effects a more speedy turnover.

For example, suppose the yearly turnover of A and B is £100,000 each: A turns over the goods in thirty days, B in 180 days; then A has an average stock of £8,333 and B one of £50,000.

From this example, it is clear that the art of conducting trade on a small capital is based chiefly on a speedy turnover. Moreover, the longer the period of warehousing, the greater the *loss of interest*.

In the above example, on the single turnover A entails a loss of  $\frac{1}{2}$  per cent. interest, whilst B loses 3 per cent. interest (i.e. A has only to account for the sixth part of that which B has to add).

In marshalling these points together, it must be concluded that the art of trade is to be found especially in a speedy turnover, not merely because the profit earned on each single turnover multiplies, but because the trading expenses diminish in the same proportion as the number of increments of profit increase. With a sixfold increase in the speed of the turnover, all direct and indirect warehousing expenses become six times smaller, whilst the return on capital outlay in the purchase of stocks becomes six times greater.

In practice, this calculation, under the influence of competition, assumes another form. The sixfold diminution of the expenses and the sixfold increase in the profit will allow the merchant in



question to act according to the principle of "Small profits, quick returns." To triumph over his competitor, he will enter the market with cheaper prices, thus affording another means of effecting a speedy turnover. Hence, it is again seen that the more economically the business is performed through a speedy turnover, the greater will be the decrease in the expenses of distributing the goods, and the more beneficial a part does trade play in the service of the producer and of the consumer.

### TEST PAPER LXIV

1. Show clearly how the increase in the warehousing period tends to raise the price of goods.

2. In what way is the period of turnover related to working expenses ?

3. "The quicker goods pass through the wholesale warehouse, the smaller is their share in the warehousing expenses." Elucidate this statement.

4. Name some commodities in which the prolongation of the period of warehousing is an advantage to the owner.

5. To what risks are warehoused goods subjected ?

6. "The art of trade is to be found chiefly in a speedy turnover." Explain this statement.

7. Given the undermentioned information, find—

(a) The percentage added to cost price to ascertain selling price.

(b) The percentage of expenses to turnover.

(c) The percentage of net profit on turnover.

Cost of goods, £10,000 ; selling expenses, £7,500 ; goods sold for £20,000.

8. A proprietor of a business has premises valued at £5,000 and stock for which he paid £3,000. He turns over his stock five times annually, making 20 per cent on his sales each time. What percentage ratio does his annual profit bear to his capital ?

### ABBREVIATIONS USED IN WAREHOUSING

Adv. . . . . Advice  
Art. . . . . Articles  
Assn. . . . . Association  
Asst. . . . . Assistant  
Ass. . . . . Assessed  
Bdle. . . . . Bundle  
Bg. . . . . Bag  
Bkt. . . . . Basket  
Brit. . . . . British  
Brl. . . . . Barrel  
B/s . . . . . Bags ; bales  
chges. . . . . Charges  
Ck. . . . . Cask  
Cts. . . . . Crates  
Ctge. . . . . Cartage  
Dept. . . . . Department  
Doz. . . . . Dozen  
D.W. . . . . Dock warrant  
D/W . . . . . Dead weight

d/o . . . . . Delivery order  
Entd. . . . . Entered  
Exd. . . . . Examined  
G. gr. . . . . Great gross (144 doz.)  
hgd. . . . . Hogsheads  
No. . . . . Number  
n/m . . . . . No marks, not marked  
(bales)  
o/c . . . . . Overcharge  
O.R.B. . . . . Owner's risk of breakage  
O.R.C. . . . . " " chafing  
O.R.D. . . . . " " damage  
O.R.F. . . . . " " fire  
O.R.L. . . . . " " leakage  
Sk. . . . . Sack  
shrtgs. . . . . Shirtings  
T. . . . . Tons ; tare  
W.B. . . . . Warehouse Book  
W.W. . . . . Warehouse warrant



## SECTION VIII COMBINES AND MONOPOLY

### CHAPTER LXV

#### THE THEORY OF MONOPOLY

**INTRODUCTION.**—At the present day, industry is influenced enormously by combinations which restrict individual freedom to a great extent. This is especially the case within the sphere of commerce, where they are the means of compelling the merchant either to subject himself in a passive manner to their power, or to join these organisations as an active member. In fact, there is no section of industry so influenced by combination as that of commerce. Hence, a knowledge of its influence forms an essential part of the study of Commerce.

It has been seen that free competition causes a tendency towards normal price ; that is to say, price is fixed at the point at which demand is just sufficient to carry off the available supply at the supply price. The absence of such freedom of competition may cause a price different from, and usually higher than, the normal price, which is known as a *monopoly price*.

Monopoly is usually due to combination on the part of the leading producers, in order to control the whole of the supply of a particular commodity, so that the supply can be increased or decreased at the will of the monopolists.

Thus, a monopoly means a control over the supply of any particular commodity, and may be either—

- (a) Complete ; or                      (b) Partial.

**COMPLETE MONOPOLY.**—If the monopoly is complete, as in the case of a patented article, where the owner of the patent has the sole right to produce the commodity, then the price is usually fixed by a calculation, that if  $x$  units of the article—each made at a cost of  $z$ —can be sold at the price of  $y$  each, then  $y$  will be so fixed as to make  $xy - xz$  as great as possible (i.e.,  $xy - xz =$  the maximum profit).



In other words, the monopoly price is so fixed as to yield the maximum net profit, neither higher nor lower, since too high a price will cause a falling off in the demand.

**MONOPOLY PRICE.**—Let the article be one which is produced under the law of increasing return, but subject to monopoly, such as a patented fountain pen. If the owner of the patent has the sole right to produce the pen, it follows that the greater the output of the pen the smaller will be the cost per unit of production, so that there may be a supply price and demand price curve, as shown in the diagram on page 802. If  $OX^1$  pens are produced, it is quite possible that when more pens are made, as, for example, at  $OX^2$ , the price may be lower and the profit greater. This will depend upon the shape of the curve as to which price will pay best to the monopolist. The total cost of making  $OX^1$  pens will be  $OS^1$ ; the total receipts will be  $OD^1$  after selling the product. It is possible that if  $OX^2$  is made at a cost of  $OS^2$  and sold at  $OD^2$ , then the profit will be  $CD^2$ . This is represented by the shaded area in the diagram, and is larger than the shaded area  $BD^1$ . Hence, it follows that it is possible for the monopolist to charge a lower price and still make a higher profit.

The monopolist has usually to find a price where, from the price of the article multiplied by the number of articles he sells is subtracted the cost of making each article multiplied by the number of articles he makes, the difference will be the maximum. In other words—

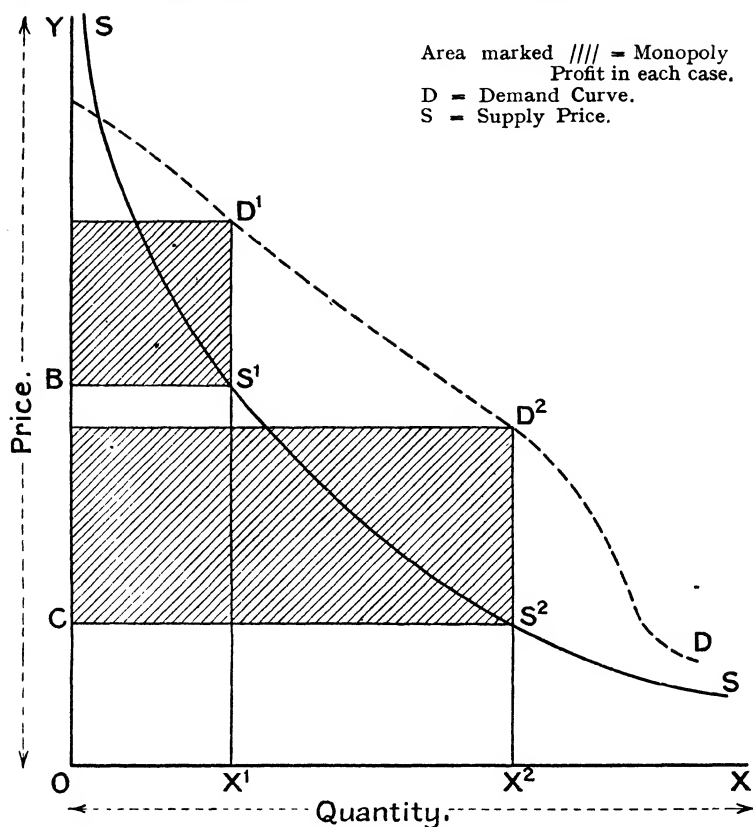
$$\begin{aligned} \text{MONOPOLY PRICE} \} &= (\text{Price of Article} \times \text{No. of Articles}) - \\ &= (\text{Cost of Production per Article} \times \text{No. produced.}) \\ &= \text{Maximum Difference.} \\ &= \text{Monopolist's Profit.} \end{aligned}$$

Wherever there is a distinct increment in gain to be found in combination, the tendency to monopoly will assert itself. The monopoly price will be fixed by the monopolist, and may be either—

- (a) The price which, in the long run, yields the greatest profit to the monopolist, or
- (b) The price which the monopolist fixes after a careful investigation of the circumstances.

The monopolist's power, however, is limited chiefly to supply, and he exercises but little control over demand. It is true there are





few instances of monopolised demand, but as a rule the power of the monopolist is based upon the fact that he can increase or decrease supply at his wish. A case of monopolised demand is to be found in the economic history of the seventeenth century, when the Government passed an Act compelling every corpse to be buried in wool. Again, in modern times, vaccination has been insisted upon by the Government, thus creating a compulsory demand for vaccine lymph.

**Partial Monopoly.** If the monopoly is based solely upon trade reputation, and is, therefore, only a partial one, the holder of the monopoly has to take care not to screw up the prices too high. If a large firm of cutlers has a great reputation for making scissors



and razors, they may charge more than other people, because they are charging for their name. If too high a price is charged, however, they will damage themselves in two ways—

- (1) They will tend to lose their customers.
- (2) Other competitors will be patronised who are able to supply a commodity of equal quality.

In reality, combinations of producers are monopolies. If it is agreed by the members of the combine that a particular article shall not be sold under a certain price, then a monopoly is established. The combination can work a monopoly as long as it is a strict combination, but it very often breaks down. Combinations between large companies having a large amount of fixed capital are rarely maintained, since the temptation to break the monopoly agreement proves too strong for some of the members. One of them may break the agreement, because he believes he can undersell the combine and thus get most of the trade for himself.

**ESSENTIAL CONDITIONS OF MONOPOLY.**—When a combination tries to keep out competition, the difficulty increases with the *portability* of the article. The confectioners of a certain town may agree to refuse less than, say, 6s. per dozen for strawberry ices, because they cannot be readily imported from a distance. A combination might also succeed in bread, but it would not be successful in calico because of its easy portability. The conditions under which a combination may most easily be established and maintained are as follows—

- (1) All the suppliers to the particular market must be included.
- (2) The combination must be strong enough to punish all delinquent members.
- (3) The commodity must be in urgent demand.
- (4) There must be difficulty in obtaining substitutes.
- (5) The commodity must be difficult to transport. No other market must be available to the consumers.

According to John Stuart Mill, it is a limitation of supply which is the essence of monopoly; but to this may be added unity of action, producing a limitation of supply, which, in turn, gives rise to an exclusive control over the article and, therefore, over price. Hence—

$$\begin{aligned}\text{MONOPOLY} &= \text{UNITY OF ACTION} + \text{Limitation of Supply} \\ &= \text{Control over Article and Price.}\end{aligned}$$



Whether the control is conferred by a Government or not is immaterial, for it is the unity of control that sets up a monopoly.

Examples of monopolies are railway companies, patents, the Post Office, etc. A partial monopoly does not mean that there is a partial control over the commodity dealt in, but that the control is exercised over a part only of the supply, and that the part of the supply controlled is not large enough to gain control over the whole field. It must also be noticed that the mere size of a business does not confer monopoly. The South Metropolitan Gas Co., for instance, holds a monopoly; but the Army and Navy Stores, which is an equally large concern, holds no such monopoly. The gas companies in London have districts assigned to them, so that they are under their control; but in the case of a large stores there is no such monopoly, because there is no part of London in which they have complete control of the commodity.

**CLASSIFICATION OF MONOPOLIES.**—Monopolies may be classified according to the owner of the monopoly, such as public monopolies owned by a political unit (e.g. the match-making monopoly of the French Government); or private monopolies owned by, and the benefit accruing to, a private person. They may be further classified according to the source of the monopoly power, so that the following division results—

(I) **Social Monopolies.** These are the result of social arrangements, and express the real will of the society. They are subdivided into—

(a) General welfare monopolies, such as copyrights, trade marks and fiscal monopolies.

(b) Special privileged monopolies, which have happily gone out of fashion. Examples are the monopolies granted to Court favourites in the sixteenth and seventeenth centuries. The re-appearance of this type of monopoly is seen in the granting of special privileges and facilities to particular firms by railway companies, amounting to what is known as an *undue preference*.

**II. Natural Monopolies.** These are subdivided into—

(a) Those arising from a short supply of raw material (e.g. limited supply of anthracite coal or of petroleum).

(b) Those arising from the nature of the business (e.g. railways and telephones). The number of railways, say, between London



and Manchester must be limited, or there would be no room to carry on agricultural operations.

**III. Secret Monopolies.** Monopolies arising from simple secrecy are more important than one is generally apt to suppose. There are firms that do not care about patenting their secret processes, because they know that the patent, when published, may be imitated without being actually infringed. Hence, a good many firms in the possession of secret processes make it clearly understood among their employees that if any information concerning the secret process is imparted to third parties, they will be instantly dismissed.

Another classification of monopolies is that which has reference to their position in the market (i.e. buyers or sellers); they may also be classified according to area (e.g. local monopoly, such as the water supply of a city; national monopoly, as in the case of the patent law of a country; universal monopoly, as in the case of the control of petroleum).

**CONTROL OF MONOPOLY.**—Although perfect monopoly is almost unknown in the sense of one supplier controlling the total output, there are numerous examples of partial monopolies of a purely local character. In certain cases it is desirable that monopoly conditions should prevail as, for example, in the case of gas and electricity, or in certain forms of transport. Where monopoly conditions exist, State interference and control will usually be called for in order to prevent the exploitation of the public. This control may be exercised in a number of ways—

(1) **By Price-fixing Legislation.** In this case the conduct of the business is left in the hands of private enterprise, but scales of rates and charges are prescribed by law. In this country, gas and railway undertakings are controlled in this way.

(2) **By Nationalisation.** In this case the control of the industry is removed from the hands of private individuals and is taken over by the State as a Government department. In these circumstances all operations are under the direct control of the Government, and the public may obtain redress for any grievance through Parliament. The only example of this type in Great Britain is the Post Office.

(3) **By Taxation.** A monopolist may be left free to conduct his business without any direct control being exerted over his actions by the Government. The profits which he makes may, however, be



subject to special taxation, thereby augmenting the revenue of the State and relieving the general taxpayer. This method may not be of general application, since it requires that the Government shall have precise information with regard to the affairs of the monopolist.

(4) **By Forming a Statutory Company.** This is a modern device which has replaced the former Socialistic idea of State nationalisation. Instead of the business being taken over and operated as a Government department, a statutory body is formed under a special Act of Parliament. This body remains free from political interference, but remains under public control on account of the special legislation governing it. This method has been adopted in the electricity supply industry and also in the various agricultural marketing boards.

### TEST PAPER LXV

1. "In every direction we see competition being replaced by regulation." Is this true?

2. Name, according to the degree of control over supply, two types of monopoly.

3. How does the owner of a complete monopoly fix the price of goods?

4. Explain by means of a diagram the meaning of "monopoly price."

5. To what dangers does a partial monopolist subject himself by raising unduly the price of his goods?

6. Under what conditions can a combination be most easily established and maintained?

7. The mere size of a business does not confer monopoly. Explain this statement.

8. How may monopolies be classified according to the source of the monopoly power?

9. What are the main forces which (a) encourage, (b) hinder, the growth of monopolies?

10. Combination is a marked feature of modern commercial life. Describe its forms and distinguish the aspects which are beneficial to society from those which are not so.

11. Discuss the maxim professed by railway companies of "charging what the traffic will bear." What does it mean?

12. "The price of monopoly is upon every occasion the highest which can be got." Comment on this statement and explain the considerations by which the monopolist is influenced in fixing prices.

13. Why has the discussion of monopoly recently acquired so much prominence?



## CHAPTER LXVI

### TRUSTS AND CARTELS

COMBINATIONS are known by different names, according to the form they assume, such as conventions, cartels, syndicates, trusts, rings, and corners. They may be divided, however, into two main forms—the cartel and the trust. A fixed meaning, however, cannot be applied to either of these terms, and frequently they are used interchangeably. The transitions from one type to the other are frequent, and take place in a variety of ways. New combinations are ever taking place, whilst existing ones are dissolved and then revived in a new form. Hence, it is better to refer to different combinations as of certain types, according as they most resemble the cartel form or that of the trust.

**TRUST AND CARTEL COMPARED.**—The main difference between the two forms of combination is the degree of independence which is left to the individual business units which go to form the combination. If a single member maintains its economic and legal independence, the combination partakes of the character of a cartel; but when such independence is lost, then the transition to the trust takes place.

In the cartel, only certain functions are centralised, and those upon the express condition that each single enterprise shall continue to exist as an independent unit. Each individual firm in the cartel relinquishes certain functions and places them into the hands of a central authority, thus securing itself against elimination by the forces of competition.

In the case of the trust, however, the whole of the functions performed by the independent units are transferred as soon as possible to the common entity, so that each is assimilated, even though it may continue to exist as a separate form in the legal sense. The effect of the formation of a trust is the disappearance of the single undertaking into a larger entity. The combination of labour, capital, and credit is effected for the purpose of increasing the power over the production and sale of the goods, and thus excluding competition from the market.

Hence, the trust goes further than the cartel. The latter aims



chiefly at the combination of enterprises in the same branch of commerce or of manufactures ; whilst the former often combines undertakings in different branches of industry, such as manufactures, trade, transport, and insurance. As it expands, it takes in competitive enterprises and grows in breadth. The trust tries to unite the largest possible number of smaller firms into one complete unit, and thus increase the production and sale of the goods ; further, it aims at adapting the output to the demand, at safeguarding the market against over-production, and at securing the most continuous uniformity of output and complete regulation of the price.

A further important difference between the cartel and the trust is to be found in their constitution and stability. Cartels consist of simple independent undertakings which combine, more or less voluntary, without yielding their rights. For them, the cartel is but the means to a certain end, viz. the maintenance of their enterprise as a profit-earning concern. Such cartels are formed by contract, lasting, as a rule, for a comparatively short time ; and each member remains in the cartel only so long as it offers advantages to him.

In most combinations of the trust type, there is evidenced the desire for self-sufficiency, and attempts are made by the trust to liberate itself from dependence on the producers of raw material, or on the sale of the finished goods. A trust which has undergone a considerable amount of horizontal expansion will, therefore, begin to develop in height and depth. The rolling mill, for instance, which has become independent of the steel works which hitherto supplied it with raw material, may start its own steel works ; and the steel works has, again, a desire in the same direction to take up its own blast furnaces. Again, the producers of pig iron may desire to free themselves from the suppliers of coal and ore, and, therefore, purchase their own coal-mines, with coke ovens, and iron-mines ; further, the trust may build its own ships, in order to become independent in regard to the transport of raw materials and of the finished products, as in the case of the American Oil Trust. Moreover, the trust may try to control the railways by buying up the shares, so that it can regulate the rates of freight in its own interest and to the disadvantage of its competitors.

The kernel of the trust is its capital, the extent of which enables



it to promote, acquire, combine, or conduct any kind of undertaking. Since the capital is organised by the large banks or financial institutions, these are generally closely connected with the trust, and are thus able to control the promotions of new businesses, the granting of credit, and can assist the trust in developing new lines which are considered by them as profitable. It is therefore clear that the modern bank exercises a great influence on the whole economic life of a country, and high qualifications are required of the leading directors in the banks. To be suitable for such a position, it is necessary that a person should have a thorough acquaintance with the money market and the various branches of industry.

**ORIGIN OF CARTELS.**—A proper knowledge of the main characteristics of trusts and cartels entails a knowledge of their origin and aims. Cartels have, with some amount of justification, been called the “children of distress.” Unrestricted competition has often led to an intolerable state of affairs, or even to the complete ruin of competing enterprises. Such competition is not always one of prices, but sometimes has reference to quality, or terms of payment, and often leads to the unrestricted production by the single business and the flooding of the market with unsaleable goods. There is only one means by which such a drawback can be overcome, viz. an agreement among the competitors themselves. Like exhausted parties in a war, they conclude peace by handing over to a central dépôt the weapons of competition, such as the fixing of the sale price, the quantity of output, etc. As a matter of fact, most cartels have originated in times of crisis or of distress in certain branches of industry.

Periods of depression are most favourable for the formation of cartels, for employers do not care to renounce part of their independence except under compulsion. When the power of the cartel increases so that it can fix the price, the danger arises of abusing its position by raising the prices to an abnormally high level. In such a case, the object is not to secure a reasonable profit for the individual members of the cartel in return for services rendered and risks undertaken, but its aim is to enrich itself at the expense of the consumers. Hence, the cartels give up the role of acting as saviours of their members from destruction and enter upon a purely capitalistic career. Such a development on the



part of cartels is specially furthered by means of protective duties, which render foreign competition impossible and thus favour an artificial increase of prices up to the point at which outside competition can enter in spite of the duties. Even this barrier may be surmounted by the formation of an international cartel.

The imposition of duties on imported goods is, therefore, one of the best means of fostering cartels which are based upon prices ; but even here there is a limit to their growth, because, by the fixing of exorbitant prices, economic forces are brought into play which lead to the destruction of the cartels.

**ORIGIN OF TRUSTS.**—The origin of trusts is quite different. They may be said to grow spontaneously out of the soil of the large industrial enterprises ; the spirit of enterprise and the power of expansion which grow with economic success lead to the conversion of the smaller enterprise into a larger one, and, finally, to the establishment of a business on a gigantic scale. Two factors favour this process—

(1) The more an enterprise develops the greater becomes its influence.

(2) Capital flows to those concerns in which the largest capital return is expected.

It would be a mistake to say that the promoters and administrators of trusts have no other idea than that of making money in their transactions. It is the spirit of enterprise by itself, the *entrepreneur's* enjoyment of the success of his own work, the intellectual pleasure of thinking out continually new ideas and of realising them, and of assisting in the triumph of mankind over nature by new achievements that contribute to the growth of such large concerns. Last, but not least, however, must be remembered the pleasure and pride derived by the employer in the development of his personal power and reputation, for this is surely one of the reasons which push most of the promoters of trusts to their goal.

**DANGERS TO CARTELS.**—The constitution of a cartel is not of a firm and enduring character, and it is threatened by the following dangers—

(1) **The Failure of its Members to Keep their Agreements.** Every member is, of course, obliged to fulfil the terms of agreement and to submit to the terms and conditions of the cartel. As security



against unfaithfulness, the cartel has often nothing more than credit documents, such as bills of exchange, which are not always acknowledged by the Courts.

The cartel is practically powerless against the secret and indirect transgression of the conditions of the cartel, which is often resorted to by delinquent members, even if agreements and terms have been most carefully and strictly drawn up so as to safeguard against such eventualities. Very often it happens that the chief cause of the dissolution of a cartel is the infidelity of its members.

(2) **The Period of Duration.** The cartel is always arranged for a certain period, such as a month or several months, but only rarely for a number of years. The question of the renewal of such an agreement is always a very uncertain matter. Especially during the last period do the members entertain the fear that the cartel will not be renewed, and in such a case they must prepare themselves at the beginning for such times when the cartel will be dissolved.

(3) **Outsiders.** The greater the participation of all enterprises of a certain kind in the cartel, the easier can it achieve its purpose of abolishing competition and of maintaining a certain level of prices.

The larger the percentage of those who do not join the cartel (i.e. the outsiders), the weaker is the cartel. For a cartel to be permanently successful, it is necessary that as many interested firms as possible should join it. However, this is a difficult matter.

In many cases, an *entrepreneur* cannot be induced to hand over important functions of his control with the simple desire of assisting other producers in the same branch of industry, and, therefore, he prefers to remain outside of the cartel until he can reap an economic advantage by joining it. There may be no necessity or compulsion to join the cartel, unless the cartel renders his position untenable by the cutting of prices in his circle of customers.

In some cases, admission into the cartel will be refused for purely business considerations. Among the competitors in any line of business are many kinds of firms—strong and weak, large and small, rich and poor. One firm may be fitted and equipped in the most modern manner, being supplied with the latest machinery and the best methods, whilst others are retrogressive. Hence, it is only natural that such weak and inefficient firms should be excluded.



For these reasons, the formation of a cartel becomes more and more difficult with the increase in the number of enterprises concerned, and also according to the extent of the differences of size, capital power, equipment, etc. It is comparatively easy for competitors to form a cartel in a certain branch of industry if they have all developed into large enterprises, and if their number is only small.

There are still other reasons, founded on economic considerations, which deter some firms from joining the cartel. In the first place, the State may legislate against enterprises in which the prices are artificially raised. Again, the power of foreign competition may be such as to overcome the barrier of Customs duties, and thus penetrate into the selling area of the cartel. Further, there are always eccentric persons who have no special reasons, but are simply obstinate and therefore refuse to join the cartel.

After considering these various points, the fact remains that nearly every cartel has to consider "outsiders" who might be a serious danger to the success of the cartel. In most cases, however, the cartel itself is able to terrorise "outsiders" and thus compel them to enter.

(4) **New Promotions.** It is only in the rarest cases that the power of the cartel becomes so great that the promotion or foundation of new enterprises can be prevented. New firms are constantly arising which compete with the cartel, especially during a period of rising prices. These new undertakings always form a source of annoyance and increasing danger to the cartel.

(5) **Dissatisfied Members.** It is clear that the individual members of the cartel consider themselves more or less hindered in their development the greater the number of functions which are taken over by the cartel. Especially is this the case if the cartel agreement arranges the quantity of output, for then the most efficient firms which would otherwise extend their works, are now prevented from so doing. Naturally, such firms demand better terms for themselves, which can only be made at the expense of the other members, and, therefore, a keen struggle ensues. If such terms are refused, these more enterprising units of the cartel may join the "outsiders" and form with them a competing cartel, or, in the last resort, they may be the means of compelling the cartel to dissolve.



The five points given above are intended to demonstrate that a cartel can be conducted only with difficulty, and that it is continually liable to dissolution. It is chiefly for this reason that so few cartels have a lengthy term of life, the constitution always being in a state of flux.

**THE ADVANTAGES OF THE TRUST.**—In the case of trusts, the position is quite different, for the individual members of which it is constituted lose their independence, and the central administration forms the governing body.

Within the trust there is no breach of contract nor cutting of prices, for all the members are linked up into one indissoluble entity. The competitive struggle is directed against outsiders, and is rendered effective owing to the possession of the advantage of a large-scale industry, such as large capital, better organisations etc. On the other hand, the management of such a concern is more difficult, and may be compared to the direction of a huge army by its commander-in-chief. Again, the *entrepreneur* has to wage warfare in order to conquer the world market, and his war implements are enormous machines which have the strength of hundreds of horse-power.

**CONCLUSIONS.**—From the social standpoint, cartels are regarded in a more favourable light than trusts, because they have as their basis the maintenance of independent enterprises; whereas, in the case of trusts, the independence of the separate units ceases to exist. From the economic point of view, however, trusts are considerably more important, since they are far more economical than the separate units of the cartel. As already stated, the cartel aims at abolishing outside competition and fixing an artificial level of prices by the preservation of weak and retrogressive firms. It is evident that this is a hindrance to the progress of industry.

The consumer sees in both forms of combination an obstacle to his own interest. Both in the trust and in the cartel, the tendency is to raise prices, to increase the profits of the *entrepreneur*, and to augment the return to capital: all of which are a disadvantage to the masses of the people. The same view is taken by manufacturers or wholesale firms which have to use the goods produced by the cartels or trusts as raw materials, for their power to compete in the world's markets is reduced on account of the increased prices charged by such combinations.



Within recent times there has been a steady transition from competition to combination in all the leading industrial nations. The movement has accommodated itself to national conditions and characteristics. In Germany and the United States it has culminated in the cartel and the trust, each in its way emblematic of the national character. In this country great consolidations have hitherto been less formidable than in America, and associations of independent manufacturers have in no single case been developed to anything like the same logical outcome as in Germany. Yet it should not be too readily assumed that British industries lag behind those of other countries in effectiveness of internal organisation. Individuality has counted for more in British manufacture than in foreign, and if amalgamation has proceeded cautiously there has been reason in the caution. British combines and consolidations may not rank as prodigies, but among them are some that can vie in efficiency with any in the world. British trade associations make little parade of their existence or achievements, but there are few corners of British industry in which some kind of trade association is not to be found, and some of them can show a thoroughness of organisation not easily surpassed. What is notable among British consolidations and associations is not their rarity or weakness as their unobtrusiveness. There is not much display in the window, but there is a good selection inside.

### TEST PAPER LXVI

1. Mention some of the different names applied to different forms of combination.
2. Into what two types may different combinations be grouped?
3. Distinguish between the trust and the cartel.
4. Account for the origin of cartels.
5. Explain the origin of a trust.
6. Enumerate the chief dangers which threaten the cartel.
7. Which is the more enduring: the trust or the cartel?
8. What are the conditions which favour the partial or complete abandonment of competition by undertakings which up to a certain time have competed with one another? Name and explain briefly the chief kinds of agreement or combination which you know.
9. Explain and illustrate the difference between so-called "vertical" and "horizontal" combinations in industry. State generally the causes which have led to each of these classes of combinations.
10. Consider the circumstances under which (a) Trusts, (b) Cartels, are likely to arise? What advantages and disadvantages accrue from their institution? Do you imagine that in the future they will become more or less general and more or less lasting?



## CHAPTER LXVII

### STAGES IN THE DEVELOPMENT OF TRUSTS AND CARTELS

**STAGES OF THE CARTEL.**—Cartels are formed for the restriction of competition and for the purpose of preventing the flooding of the market with goods and the consequent sudden fluctuations in prices. Cartels are weapons in the sphere of sale with regard to the period of payment, the quality and the prices of the goods. The following are the stages of development—

(a) **Condition Cartel.** The first step is a Condition Cartel, based on an agreement among the members to grant to consumers no preference terms or conditions with regard to time of payment, discount and allowances, or mode of delivery. If a member of the cartel acts against such a contract, a penalty is imposed. This first stage is not very effective, but it may be instrumental in removing the worst evils of competition.

(b) **Quality Cartel.** The cartel which is based on an agreement with regard to the quality of goods has to fix a definite standard for various qualities and grades of the commodity sold, and has to prevent a better or worse quality being delivered secretly by any of the members. Among these are cartels for the determination of uniform prices, as for the various grades of cotton yarn, silk, wool; also in regard to sugar, coal, or iron. The differences of prices between the various qualities have to be fixed and are binding on all vendors. There is a large number of products where a uniform fixation of the quality is not feasible, so that in such cases this form of cartel is not possible.

(c) **The Price Cartel.** The most important weapon in the competitive struggle is undoubtedly the price. The above two forms of cartel do not offer very great advantages in this respect, so that there has arisen the price cartel which includes the first two forms. In fact, price cartels excel all other forms, so that the term "cartel" generally means a price cartel if no further explanation is given.

Price cartels are subject to many disadvantages, and are, therefore, rarely of a lengthy duration. In the first place, there are many opportunities, especially for the travellers and agents



of the various units constituting the cartel, to evade the terms and conditions of the cartel agreement. Again, the selling price fixed for all members leaves an unequal margin of profits for each firm, because they have different expenses of production. Hence, one firm may make a large profit, whilst another makes practically none. The consequence of this is, that the large producers who desire an expansion of their business, endeavour to free themselves from the cartel; or it may happen that one firm can supply at the same prices better quality than the other, especially in manufactured goods. The result is that one takes customers from the other by supplying better goods, because it takes from him the opportunity to equalise the lower quality of his goods by a reduction of prices. In such a case, the smaller firms with less efficiency consider themselves threatened by such a cartel and demand dissolution. The price cartel does not restrict production and, therefore, cannot prevent an overstocking of the market; on the other hand, the artificial increase of prices means a reduction of consumption, so that price cartels may often lead to a crisis. The reaction on the enterprises in the cartel is seen in the irregularity of the sale. Hence, the price cartel is unable to mitigate the struggle for customers, which is the keenest in competition, and, therefore, more far-reaching forms of cartel have to be employed.

(d) **Cartel for the Protection of Customers.** Among such higher-grade cartels is to be included the cartel for the protection of the selling area or circle of customers. It consists in the obligation of the members, under high penalties, to limit their selling area to their former customers or to undertake not to penetrate into the spheres occupied by other members of the cartel. Examples are to be found in railways, shipping and forwarding concerns, which sometimes make agreements to restrict their operations to certain districts or to abstain from competition in the districts of the others. Forwarding agents often arrange with their competitors that each of them shall retain a certain branch of business without competition.

Such cartels can be of a lasting nature only if all competition on the part of outsiders is excluded, and when the branch in question is practically a monopoly.

(e) **Cartel for the Sale of Goods.** None of the above-mentioned cartels can exclude competition for a lasting period. This is only



possible if the whole processes of selling are taken out of the hands of the single individual members and entrusted to centralised headquarters. In such a case, the individual merchant or producer is called upon to renounce one of the most important functions of his work if he relinquishes the whole of the selling operations. Hence, these cartels are rarely met with except in regard to certain products which are specially suitable for such treatment.

An arrangement to establish central headquarters of sale cannot be effected successfully for short periods, but it must assume a legal form and an organisation capable of obtaining credit and executing commercial operations in general. As a rule, the form assumed is that of a limited company. The members of such a cartel are thus enabled to specialise on the side of production, since they are relieved of such duties as finding customers, fixing prices, giving credit to purchasers, and obtaining payments.

*(f) Cartels for the Limitation of Output.* Again, these combinations could not exist permanently if each member had the liberty to enlarge his business indiscriminately and thus increase the output. The central sales association may be organised in the best possible manner, but it will not be able to sell unlimited quantities of goods produced by the members. If this were permitted, the market would soon be overstocked, the goods would remain unsold, and a crisis would be the result. Hence, a further function has to be exercised by the headquarters of sale, viz. the limitation or determination of the quantity of output on the part of each member, which depends on the fluctuations of the total sales. Since the profit of each separate enterprise depends upon the extent of its output, each member demands the greatest possible share of the total output, the arrangement of which is a source of trouble on the renewal of the cartel agreement.

Conflict often ensues among the various members of the cartel with regard to the allocation of the output. This is natural, since the enlargement of a separate concern can take place only by an increase in the total output and a consequent increase of the fraction assigned to the single firm. It may happen, however, that one member of the cartel may acquire by purchase the quota of another member. Such conditions prevail in most cartels, and it often happens that members buy the quota of other works, not



for the purpose of continuing the concern, but to have its share of production transferred to their own works.

The organisers of a cartel are apt to abuse their power in the fixing of the price of the goods so as to enable a large profit to be realised at the expense of the consumers. It is evident, however, that even the highest stages of the cartel are incapable of permanently safeguarding the members against competition. This is the reason why the combination often develops beyond the cartel in the direction of the trust.

**STAGES OF TRUST DEVELOPMENT.**—The highest form of the cartel, viz. the centralised headquarters of sale with a restriction on the output, differs but slightly from the loosest form of the trust. Trusts represent a much higher form of combination, because the single firms lose their independence if they are combined in a trust. There is no object served in the development of particular interests, because each unit is now subjected to the interest of the whole. The administration, the capital, and the profits are united for one object ; and, therefore, the single individual firms have no particular interests to pursue even if they should retain, *prima facie*, their old firm name.

It is possible to distinguish the following stages in the development of a trust—

(1) **Pool.** The loosest form of trust is known as a *Pool*. In this case, the combined firms which formerly competed with each other agree to club together their profits and then distribute them on some basis previously decided upon. If such combinations were of an enduring nature, they would undoubtedly constitute an ideal form of trust. In the first place, they permit each member to retain his own independence and, in the second place, they remove competition by the combination of their profits. Experience teaches, however, that such associations have, for various reasons, no lasting durability. As each firm in the pool continues to exist on the same scale as formerly, there is no reduction in working expenses, and, therefore, the economic principle is not realised. Moreover, the vitality of the individual firms is to a certain extent paralysed, and they soon become unable to withstand the competition of outsiders. The chief examples of pools are to be found in the sphere of transport in the United States, England, and Germany.



(2) **Community of Interests.** Similar to a pool is a "*Community of Interests*," which has been tried repeatedly in a loose form. This loose form consists in an understanding between the various firms to avoid further competition and to assist each other by the loan of capital, and the clubbing together of the profits, which are afterwards shared in a certain proportion. This union of interests may be strengthened by one company acquiring the shares or majority of shares in another company without taking over its control, so that it continues to exist in its own name.

(3) **Compulsory Exchange of Shares.** Closely connected with the last-mentioned form is the compulsory exchange of shares of the various companies in the trust amongst each other. Each company increases its share-capital and hands over the new shares in exchange for new shares issued by another company in the trust.

(4) **The Modern Trust.** The modern trust buys the majority of shares in a number of separate undertakings, and brings them under a new body in the form of a new limited company. In this way, a complete and absolute control is obtained over all the members.

These various forms of association cover by far the greater part of the whole field of that industrial combination in the United Kingdom which results in the concerted regulation of trade, but they are not quite exhaustive. There is still to be mentioned the control exercised over output and prices by the interchange of shares between nominally independent and competing companies almost invariably accompanied by arrangements whereby directors of one concern sit upon the board of the other. Numerous examples of this are to be found in the coal-mining industry. Neither has anything here been said of local associations of retailers, of merchants' associations and alliances, of the multiple shop system, of the tied-house system in the licensed trade, of the recent great amalgamations in the financial world, of the control exercised over tobacco, meat, and other commodities by interests outside the United Kingdom, nor of the rings and conferences in the shipping industry.

#### TEST PAPER LXVII

1. Enumerate the different stages of the cartel.
2. What is a pool?
3. State the chief stages in the development of a trust.



# SECTION IX—COMMERCE AND THE STATE

## CHAPTER LXVIII

### LOCAL GOVERNMENT AUTHORITIES

**NATURE OF THE LOCAL AUTHORITY.**—Local government authorities are compulsory organisations subordinate to the central government, existing for the purpose of discharging the functions of government which are the particular concern of the inhabitants of a given locality. A local authority has been defined in the Finance Act, 1931, as “any body having power to levy a rate or to issue a precept to a rating authority and includes the corporation for which any such body acts for executive purposes.”

The functions of local government have been defined as those “which concern life, liberty, and the pursuit of happiness.” The local authority is charged with the performance of many duties which contribute materially to the welfare of the individual. These local services are on the increase, for since the War there has been a steady stream of legislation giving local authorities fresh powers and imposing fresh duties and obligations upon them. Neither Parliament nor the Cabinet can undertake much more work: local government is the only form of democratic control not yet over-burdened: and there is reason to expect that Parliament will impose yet further compulsory services on local authorities. The *principal functions* which these bodies now perform have been stated by J. J. Clarke in *The Local Government of the United Kingdom* (Pitman) as follows—

(a) Maintenance of a local legislature, with power to make by-laws which are a code of detailed instructions for the application locally of the general principles of law.

(b) Care of certain classes of the community, e.g. the destitute.

(c) Provision of arrangements for public safety.

(d) Maintenance of works of public convenience and utility.

(e) Establishment of institutions for the betterment of the community, and for the development of character.

(f) Management of quasi-commercial undertakings.

(g) Power to raise money either by a system of rating or by one of loans repayable over a period of years.



**FORMS OF MUNICIPAL ENTERPRISE.**—Municipal enterprises now assume a diversity of forms and show a continuous tendency towards expansion. Municipalities no longer confine themselves solely to the establishment of institutions which cannot be carried on by private entrepreneurs, but to some extent they also occupy themselves with the production or distribution of goods, that is, they create their own *public undertakings*, and thus displace the private undertaking. The following types may be distinguished—

(1) **Municipal Institutions.** These are municipal enterprises which are not administered from a purely economic standpoint, but are created for the discharge of what have been termed the “political” functions of local government. These services, whether they be exclusively for the common good, as, for example, the provision of police, the maintenance of high roads, or the lighting of the public streets, or whether they be partly for the common good and partly for the welfare of particular individuals, as, for example, the relief of the destitute and the free education of children, are paid for entirely out of the funds provided from the rates or by taxation. Certain services fall under this heading, too, even though they yield a certain revenue. Thus, an Education Committee which charges admission fees to its secondary schools, or a Sewage Committee which sells grease and clinkers are not regarded as trading enterprises, in view of the fact that the functions performed are largely political, and the vast bulk of the expenditure of these departments has to be met out of the rates or from taxation.

(2) **Subsidised Undertakings.** These are economic undertakings where the products or services are paid for by the consumers as such. From various motives, however, it has been decided that these undertakings need not be entirely self-supporting, but shall receive a subsidy from the rates. This course of action often occurs on sanitary grounds, as in the case of swimming baths, where a high charge for admission would be necessary to make them self-supporting. This would deprive the poorer classes of access to adequate bathing facilities. Another motive may be the general welfare of the community which may act as a justification for subsidising municipal dock and harbour undertakings or places of amusement in health and pleasure resorts. Another reason for which municipalities sometimes subsidise undertakings is to encourage the intellectual life of a town. It is on this ground that municipal theatres are



established on the continent of Europe. In large towns, like Frankfort and Lyons, there are two municipal theatres, the one devoted to opera, the other to drama.

(3) **Trading Enterprises.** These are undertakings which are regarded as strictly trading enterprises, to be managed on a self-supporting basis. They may include such enterprises as gas-works, water-works, electricity, tramway, and light railway undertakings, in respect of which it is requisite to arrive at an accurate statement of profit and loss. Municipal trading undertakings may be monopolistic in nature or they may be faced with outside competition. The monopolisation of public utility services such as gas, water, or electricity by municipalities has created but little opposition, since it is clearly in the interest of the community. It would never pay in an average-sized town to have two undertakings supplying such services, because of the large amount of capital involved and the high overhead costs. When, however, the municipality embarks upon ordinary commodity trading this justification is no longer present, and other motives must exist to warrant such intervention where a local authority comes into direct competition with its own ratepayers.

**CAUSES OF DEVELOPMENT OF MUNICIPAL UNDERTAKINGS.**—A variety of motives has led to the extension of the field of municipal enterprise in the sphere of economic activity. There are those who would wish to see the socialisation of all the essential services, and who regard the extension of municipal control as a step in this direction. It is, however, well recognised that the various forms of enterprise have their appropriate scheme of organisation most nearly suited to their needs, and that, amongst others, municipal enterprise plays its part. Amongst the various motives may be recognised the following—

(1) **Existence of Monopoly.** Certain industrial undertakings possess a strong tendency to become monopolies owing to the nature of their business. Some of these industries, such as railways, telegraphs, and telephones are national in their scope; others, such as water, gas, and omnibus services, are local. All industries of this type require the investment of a large amount of capital throughout the area which they serve, in order to distribute the product or service which they supply. As soon as one such undertaking has laid its mains or its lines in a district, no direct competitor is likely to enter the



field, as it is improbable that the population of the district could support two similar undertakings. One reason for which water, gas, and similar services have frequently been municipalised in preference to adopting an alternative method of control lies in the fact that they all involve certain rights in connection with the public streets. Mains, and lines must be laid and kept in repair, and this cannot be done without pulling up the streets and obstructing traffic, and many local authorities feel that this should be under their entire control. Again, many of these services are more or less necessities, and to a very large extent the body of consumers coincides with the body of ratepayers. This being so, the local authority for the purpose of providing water, gas, and tramways, may be regarded as a society of consumers who unite to provide themselves with certain necessities of life with a view to saving the profits of the middleman.

(2) **Capital Expenditure.** Many enterprises may be municipalised, since heavy capital expenditure is called for which will yield no revenue for a long time. This argument applies most strongly to the supply of water, where considerable foresight is required. In a year or two the output of most ordinary undertakings can be doubled or trebled, but to secure an additional supply of water to a town ten or more years of continuous work may easily be required. This means that for several years a large amount of capital will be unproductive, thus seriously affecting the profits of the undertaking and making boards of directors very reluctant to enter upon any large scheme. Again, in the case of transport facilities, for example, it may be necessary that extensions of an unremunerative kind shall be undertaken for social reasons. Thus it may be desirable to offer special facilities to certain parts of a town with a view to inducing people to live farther out, and relieving congestion in the centre. This may be done by charging especially low fares on certain routes.

(3) **Public Interest.** In many cases the most obvious reason for embarking upon municipal undertakings is simply the fact that there is an unusually great public interest shown in this or that service, and it is believed that the best interests of the public would be served by a municipal undertaking. In industries closely associated with the public health, where reliable quality is essential, and where inspection cannot easily be made thorough, public operation



may be desirable. Thus, there is much to be said for the public provision of slaughter-houses, to which, as in Germany, all butchers are compelled to resort. In many cases, however, the appropriate remedy lies not in municipalisation, but a more rigid enforcement of regulations affecting the industry in question.

(4) **Raising Revenue.** A further reason for municipal trading operations is to secure for the local authority the profits resulting from them. One reason why many local authorities are anxious to obtain sums in relief of the rates is that the great bulk of the revenue has to be obtained by direct levies in the form of rates on land and buildings. Consequently, if some revenue can be obtained from what amounts to indirect taxation, the burden is not felt quite so severely. If people pay a slightly higher price for their gas or travel a somewhat shorter distance on a municipal vehicle for a penny, they do not feel it in the same way as if they had to pay higher rates.

(5) **Cost of Management.** Another consideration which may lead to an extension of municipal trading is the saving in the cost of management in the case of public, as compared with private, ownership; there are no directors' fees to be paid, and the salaries of municipal officials may be lower than those of private undertakings. The saving, however, may easily be more apparent than real. The fees paid to directors of companies are often small when compared with the increased earning capacities of the companies due to their efforts. On the other hand, the unpaid aldermen and councillors who constitute the trading committee of local authorities may contribute little or nothing to the success of the undertaking for which they are responsible, and sometimes may even cause it to be less successful than if the management had been left entirely in the hands of the officials. Again, it is frequently alleged that local authorities fall into the temptation of over-staffing their undertakings.

**REVENUE AND EXPENDITURE.**—Municipal administration embraces the methods by which the means are raised for the carrying on of the public organisation, and, further, the manner in which these means are spent. Since the municipality is not, strictly speaking, a trading concern, it has to procure the means necessary for its management in a different manner from the private business. As the municipality is a compulsory organisation supported by the State, it is in a position to force its members to contribute according

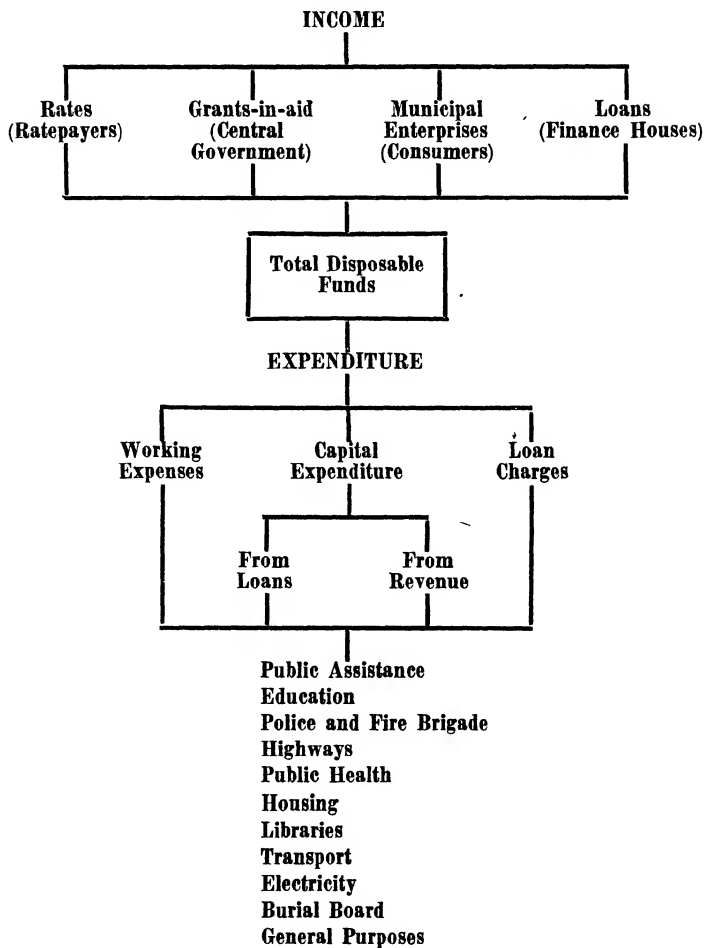


to the needs of the municipal administration. The principal sources of revenue are—

(1) **Rating.** This is a form of local taxation the proceeds of which are applicable to local purposes of a public nature, and which is leviable on the basis of an assessment in respect of the yearly value of property. The power of municipalities to levy rates is restricted and regulated by the State under the Rating and Valuation Acts. Furthermore, although local expenditure is decided upon by local authorities as far as matters of secondary importance are concerned, the State decides upon the principal items. Local rates have two characteristics which make a study of their effects on industry more necessary than in the case of national taxation. The first is that rates enter into the cost of production. Rates are payable whether a profit is earned or not; they therefore form part of the fixed costs which must be allowed for in the price. The second is that rates vary, often considerably, between different areas, and may have effects upon the localisation of industry. The derating provisions of the Local Government Act, 1929, granted relief to certain classes of industrial property.

(2) **Grants-in-aid.** This is a subvention payable from the Exchequer of the United Kingdom to a local authority in order to assist it in the execution of some or all of its statutory duties. The subvention may be an isolated payment, but is usually recurrent or annual. It may be a matter of statutory obligation or dependent upon the recurring decision of the Minister in charge of a particular department. It may be unconditionally of fixed amount, or variable according to the circumstances of the time. Most important of all, its variable amount may be dependent upon the growth of population, or of a particular section of it, on the amount of some particular service, on the number of officers appointed, or the sum of their salaries, on the expenditure of the receiving authorities, on the efficiency of its work, or some other condition. The principle of transferring a portion of the cost of locally administered services to national taxation has been adopted in recent years on an increasing scale. This is justified by the fact that many functions of local authorities are national services locally administered. The grants have had the advantage of relieving the rates, while there has remained on the local authority sufficient responsibility to secure economical administration. Further, the control gained by the



**INCOME AND EXPENDITURE OF A MUNICIPALITY**



Government owing to its power to withhold the grant has been of great benefit in securing a higher standard of efficiency.

(3) **Revenue from Municipal Undertakings.** As already indicated, many forms of municipal activity create a revenue. In certain cases, this revenue may meet but a small fraction of the total cost of the service, whilst in other instances it may more than cover it. In the latter case, the municipal trading undertaking may show a surplus of profit which can be utilised for the relief of rates. In certain cases, however, an exaggerated value is placed on revenue from such sources, since the so-called surplus is a fictitious one. It may be obtained as a result of making inadequate provision for depreciation, or by reason of the fact that other departments of the municipality are giving services to the trading undertaking either for nothing or much below cost.

(4) **Loans.** A local authority may raise money by borrowing in order to undertake works of public utility which could not be paid for out of current revenue without imposing an onerous burden upon the present body of ratepayers. Except in certain special cases, local authorities have no general authority to raise money by way of loans. Their borrowing powers are limited to the provisions of statute law, which also regulate their loan procedure. In giving sanction for borrowing the Department concerned stipulates the period in which the loan must be repaid, the number of years approximating as closely as possible to the estimated minimum life of the work upon which such expenditure is being made. The obligation is, therefore, upon the corporation to set aside each year enough money which, accumulated at compound interest, would produce the amount borrowed at the end of the period stated.

### TEST PAPER LXVIII

1. Name the chief bodies that administer the local government of England and Wales. What are the principal functions which these bodies perform?

2. Show clearly the type of enterprise that might be efficiently organised by a municipal corporation, and give three concrete examples.

3. "A variety of motives have led to the extension of the field of municipal enterprise in the sphere of economic activity." Specify these motives.

4. Discuss the relative advantages and disadvantages, from the social point of view of municipal and private enterprise in industry. Illustrate your answer, as far as possible, by reference to any enterprise of which you have made a special study.

5. What are the principal sources of revenue of a municipality? For what main purposes is this revenue utilised?

6. Draw the diagram on page 826 and explain its meaning.



## CHAPTER LXIX

### CENTRAL GOVERNMENT DEPARTMENTS

**FUNCTIONS OF GOVERNMENT.**—In 1776 Adam Smith wrote his great work on *The Wealth of Nations*, which was intended to argue that the functions of the Government should be very strictly limited. One aspect of his writings taught that every man may and every man must live to mind his own business. According to him, there were only three ruling functions for the Government to attend to—

(1) The protection of all its citizens from external force or fraud ; that is to say, the maintenance of an army and a navy to protect each community against the possible aggression of some other community.

(2) The protection of each against force or fraud of others ; that is to say, the maintenance of law and order, the administration of justice and of an effective system of police.

(3) The provision of other conveniences. What it is the interest of everyone to attend to, generally leads to no one attending to it. For example, it is to everybody's advantage that there should be lighthouses round the coast, and still it is no particular person's duty to provide such conveniences. Therefore, it is the duty of the Government to interfere and make the provision.

John Stuart Mill endeavoured to classify the functions of Government into two great classes—

(1) The necessary ; and

(2) The optional.

This classification is not very definite, for the necessary functions of Government simply mean the duties which every civilised community has, in fact, undertaken. Among these are the maintenance of law and order, army and navy, etc. ; whilst the optional functions are those which, as a matter of fact, sometimes are and sometimes are not carried on by the Government. An example of an optional function is the maintenance of the railways, because some countries carry on the railways as Government undertakings, whilst others leave them to private enterprise. Sometimes a function which has been regarded as necessary passes into the optional class,



and vice versa. . For example, almost every authority regarded the function of coining money as a necessary function, but this was challenged by Herbert Spencer, who held that the work of minting would be better done by private enterprise.

Of late years, England has tended to entrust a great many more functions to the Government than was formerly the case. Within the last thirty years the tendency has undoubtedly been to look more and more to the extension of Governmental interference, and this is especially the case in the realm of Industry. The control of industry by the Government during and since the great European War is too well known to require further comment.

The State may consider it expedient to make regulations to control business from the point of view of any one or more of the various interests concerned, and those interests are all more or less antagonistic to each other. The chief of these are—

(1) The investor who has capital in a particular kind of undertaking ;

(2) The worker employed in it ;

(3) The customer who looks to the undertaking for the supply of certain goods or services ; and

(4) The community as a whole whose interest, though less direct, is not necessarily less important.

At various times and in various ways, the State has intervened in the interests of some one or more of these different classes. Directly such intervention takes place, there is an interference with the freedom of contract ; otherwise the intervention is of a purely ornamental character.

Because all intervention must interfere with individual freedom of contract, it is sometimes argued that it must necessarily be a bad thing in the long run, although this does not always follow. Freedom of contract suggests a certain amount of option to both contracting parties to deal elsewhere, and in England it is usually considered inadvisable to interfere with this freedom unless the limits of the consequences of the intervention can be foreseen. It must be remembered, however, that competition is not altogether an unmixed good, but that it is attended with certain disadvantages. There is in many cases a tendency to increased prices, since competition involves a certain amount of waste due to friction between the competitors, so that, in



many cases, something may well be said in favour of restricting competition.

**GOVERNMENT DEPARTMENTS.**—State control may be exercised through Government Departments or through local authorities. The most important Government Departments which exercise any control over commerce are as follows—

- (1) The Board of Trade.
- (2) The Ministry of Health.
- (3) The Ministry of Transport.

**The Board of Trade.** This department of the Government is the nearest approach in England to a Ministry of Commerce, which has so often been mooted.

The Board of Trade is organised in two main divisions or departments, viz. : The Department of Commerce and Industry, and the Department of Public Services Administration. The former is mainly concerned with the development of trade, with vigilance, with suggestion, with information and with thinking out and assisting industrial policy. The latter is chiefly engaged in the exercise of statutory and other administrative functions of a permanent nature with regard to trade and transport.

**DEPARTMENT OF INDUSTRY AND COMMERCE.** For greater efficiency in working the Department of Commerce and Industry is divided into a number of sections : i.e.—

(a) *Commercial Relations and Treaties.* This section deals with such matters as commercial treaties and agreements, Empire and foreign tariffs, and matters relating to the protection and furtherance of British commercial and shipping interests in the Empire and in foreign countries.

(b) *The Mines Department* was established by the Mining Industry Act, 1920, for the purpose of securing the most effective development and utilisation of the mineral resources of the United Kingdom and the safety and welfare of those engaged in the mining industry.

(c) *Overseas Trade (Development and Intelligence).* This is a joint department of the Board of Trade and the Foreign Office and, so far as the Board of Trade is concerned, it is a centre at which information on all subjects of commercial interest is collected and classified in a form convenient for reference. Information on the following subjects is supplied, viz. : Foreign and Colonial contracts,



and other openings for British Trade, lists of manufacturers engaged in particular lines of business ; tariff and customs regulations ; statistics, certificates of origin ; regulations concerning commercial travellers ; sources of supply, prices, etc., of trade products.

One other section of the Department of Overseas Trade is the Exhibitions and Fairs Division, the main function of which is to organise the British Industries Fair, held annually at London and Birmingham. The chief purpose of this Fair is to propagate knowledge of British goods and so widen their market at home.

The Overseas Trade Department has now at its disposal for the purpose of obtaining commercial information and of assisting British commerce generally a much more comprehensive organisation than has ever previously existed. It is divided into two sections—geographical and trade. The first of these consists of officers with specialised knowledge of particular markets, while the second is staffed by officers specialising in groups of commodities, who are in contact with the particular industries of this country. The main function of the Department is to bring to the attention of British manufacturers not only specific openings for the export trade which come to their notice, but all general information of a commercial or economic nature which may be of assistance in their trade abroad. All information received by the headquarters office from its overseas officers is brought by that office before the trading community by direct dissemination or by publication in the *Board of Trade Journal*.

The work of the Department of Overseas Trade at home is supplemented abroad by that of Trade Commissioners and the Commercial Diplomatic Service. Trade Commissioners were appointed in 1908 in Canada, South Africa, Australia, New Zealand and India as a result of recommendations approved by the Colonial Conference in 1907. In other parts of the Empire the Department has the assistance of Imperial trade correspondents, while the members of the Commercial Diplomatic Service are appointed for service in foreign countries. Both Trade Commissioners and Commercial Diplomatic Officers furnish reports on the economic conditions of the countries in which they serve, and these reports are published in a regular annual series. Apart from the work of distributing information, the Department and its officers are able in many ways to help British firms in connection with difficulties which they may be



experiencing in providing their representatives with facilities when paying business visits abroad.

(d) *Industries and Manufactures*. The work of this branch has special reference to the development and stability of home industries, to production, and to the economic strength of the country generally. It also deals with questions of policy connected with trade monopolies and combinations, alien penetration into British industries, and the promotion of new trades.

(e) *The Standards Division* is responsible for the custody of the Imperial and secondary standards of Weights and Measures, and deals generally with matters arising under the Weights and Measures Acts.

(f) *Industrial Property*. The main function of this section is to administer the law relating to patents, designs, trade marks and copyright ; to encourage invention, and protect the public from the abuse of monopoly. It also advises on international questions relating to the protection of British traders against infringement of their rights in foreign countries.

(g) *Industrial Power and Transport*. Questions of general policy relating to transport in its commercial aspect, including shipping, canal and railway rates and facilities, through railway and ocean rates, shipping conferences, etc., are the chief concern of this section ; which in addition deals with questions of policy relating to electricity, gas and water power for industrial purposes.

(h) *Statistics*. Among other matters, the duties of this section include the preparing of British and foreign import and export returns ; the compiling of statistics relating to shipping, railways, prices, emigration and immigration, output of industrial establishments ; and the studying of statistical data relating to the progress of trade, industry and transport, both at home and abroad.

(i) *Intelligence and Parliamentary Branch*. The duty of this section is to study systematically the general economic position of the country and the problems arising therefrom.

DEPARTMENT OF PUBLIC SERVICES ADMINISTRATION. The chief work of this branch of the Board of Trade is the administration of a number of important Statutes relating to Shipping, Companies, Bankruptcy, Weights and Measures, etc. The activities of the various sections are indicated in the following paragraphs—



(a) *The Marine Department* administers the statutory provisions regulating merchant shipping and seamen, and is responsible for dealing with safety of life at sea, registry and tonnage of ships ; the examination of masters, mates, engineers and fishermen ; the engagement, discharge and payment of seamen ; inquiries into wrecks, etc. A sub-department keeps the registers of ships, issues certificates to officers, and has custody of official logs, agreements, etc.

(b) *The Companies Department* is responsible for the administration of the acts relating to Joint Stock Companies, and has duties under the Registration of Business Names Act, the Assurance Companies Act, 1909, etc. It also exercises supervision over Official Receivers connected with the winding up of companies.

(c) *The Bankruptcy Department* is responsible for the administration of legislation relating to Bankruptcy and Deeds of Arrangement and exercises supervision over Official Receivers in Bankruptcy.

**MINISTRY OF HEALTH.**—Through the Ministry of Health, which took over (among other things) the functions formerly performed by the Local Government Board, there is a certain amount of intervention, direct and indirect.

The direct (i.e. that which is exercised by the Ministry of Health itself) is, primarily, the financial control over local authorities. In particular, the local authorities can borrow nothing without the sanction of the Ministry of Health, and, in many cases, the local authorities have to submit their accounts to auditors appointed by the Ministry of Health, who go through them with a view to seeing that everything is in order ; and particularly in order to see that nothing has been spent or borrowed without the necessary permission having first been granted. If there were no such safeguards, there might be serious abuses.

Indirectly, the Ministry of Health, working through local authorities, operates in various ways which certainly impose restrictions on business. One example is the administration of the *Factory Acts* and *Shop Acts*. Broadly speaking, the general tendency is the same in both cases—to limit the number of hours which persons may be employed, and, in the case of the *Factory Acts*, to some extent to ensure that they are employed under sanitary conditions. In this connection, the *Factories Act, 1937*, is an important mile-



stone on the road to safety, health and welfare in industry. It marks the notable progress made in the twentieth century and shows in its up-to-date provisions what should be done to secure a further reduction in the toll of accidents and sickness, and a general advance in the conditions of factory life.

**MINISTRY OF TRANSPORT.**—The *Ministry of Transport Act, 1919*, established a Minister of Transport for the purpose of improving the means of, and the facilities for, locomotion and transport. There were transferred to the Minister all powers and duties of any Government Department in relation to (a) railways; (b) light railways; (c) tramways; (d) canals, waterways and inland navigations; (e) roads, bridges, and ferries, and vehicles and traffic thereon; (f) harbours, docks, and piers. The Minister may establish, and either by himself or through any other persons may work, transport services by land or water. He also administers the Road Fund, a fund kept separate from the country's main revenues, fed by the proceeds of taxation of motor cars, and devoted to the upkeep of the roads. Under the Road Traffic Act, 1930, control of district omnibus services is vested in the Traffic Commissioners of the Ministry. The Ministry is also responsible for the exercise of the Government's powers and duties dealing with electricity and for general questions relating to the Electricity Commission and the Central Electricity Board. For the purpose of giving advice and assistance to the Minister, advisory panels, including representatives of local authorities, are set up, and a Rates Advisory Committee.

**STATE REGULATION OF ACCOUNTS.**—The next aspect of State control is with regard to the statutory provision for the preparation and publication of accounts by certain undertakings on uniform lines. This provision is spread over a variety of different kinds of undertakings without any very definite underlying principle being observable. Uniform accounts are required in the case of railway companies, gas companies, most water companies, electricity companies, insurance companies, building and friendly societies, and the smaller local authorities. In some cases, the precise form of accounts is embodied in the Act of Parliament, but in other cases the Act provides the authority which is to decide what the form is to be from time to time. Thus, in the case of railways, gas, and insurance companies there is a statutory



form, but in the case of electricity companies the Board of Trade from time to time decides what the form is to be.

In the case of building societies and friendly societies, the Registrar of Friendly Societies decides what the form is to be ; and in the case of local authorities it is decided by the Ministry of Health. The appointment in this manner of some prescribed authority to modify the form from time to time is probably the better method, for there is more chance of the form being kept reasonably up to date.

It is not easy to see why the State prescribes forms of account for these particular undertakings and not for others, but whether it makes any great difference one way or the other may be doubted, for the uniformity in all cases is a merely superficial one. That is to say, the uniformity is confined exclusively to the form of the published periodical accounts of these concerns, and in no way touches upon the way in which those accounts shall be kept. The prescribed forms of Balance Sheets and Revenue Accounts, etc., do, of course, make for convenience in comparing the results of one undertaking with those of another in a similar line of business, but this case is, again, but a superficial one. There is little assurance that the various headings prescribed in these forms are interpreted alike by all the different concerns adopting them, or even that any one concern has adopted the same interpretation of the headings throughout the whole of its career.

### TEST PAPER LXIX

1. What, in your opinion, are the functions of Government ?
2. Discuss, from an economic standpoint, the circumstances which render an industry suitable or unsuitable for public management.
3. What are the chief duties of the Department of Industry and Commerce of the Board of Trade ?
4. State in a general way the chief functions of the Board of Trade.
5. Describe the assistance rendered to business men engaged in overseas trade by the Department of Overseas Trade.
6. What restrictions are imposed upon business through the Ministry of Health ?
7. Mention some of the cases where the State regulates by statute the preparation and publication of accounts.
8. Give a brief account of any measures known to you by which, in recent times, the Government has intervened for the purpose of promoting or facilitating the trade and industry of the country.



## CHAPTER LXX

### CONSULAR AND OTHER GOVERNMENT SERVICES

THE rise of the Consular service coincides with the early beginnings of commercial intercourse among European peoples. The first reason for the establishment of such an institution was the need for the protection of persons engaged in the conduct of trade with overseas factories and trading centres, and from this there has gradually developed the present significance of this institution.

**DUTIES OF A CONSUL.**—A Consul is a person appointed by his Government to reside in some foreign country, in order to watch over and further the commercial interests of the nation he represents. Every Government maintains a consular service and has a Consul-General in each foreign country of importance, with Consuls and Vice-Consuls in the principal commercial centres. The British service was reorganised after the Great War, and has been under the control of the Department of Overseas Trade since 1919. From this time greater stress has been laid on the commercial side of its work. It is now divided into three branches: *The Far Eastern*, covering Japan, China, and Siam; *The Levant*, covering Turkey, Egypt, Morocco, Syria, Persia, Russia, Greece, and Bulgaria; and the *General*, covering America and countries in Europe and Africa not included in the Levant service. Entrance to the service is by competitive examination. Prospective candidates must first of all appear before a board of selection which meets at the Civil Service Commission, 6 Burlington Gardens, London, W.1, in May of each year.

A British Consul helps to protect the interests of British subjects who may be residing in his district. He is expected to assist them if tried for offences, and to see that they are not inhumanly treated on being convicted. He has power to make inquiry upon oath concerning all offences committed by British seamen on the high seas, and to give assistance to shipwrecked and unemployed seamen and other destitute persons, and to provide them with the means of returning home. He issues passports to British subjects, celebrates marriages between them, and generally does his best to further their interests. Some of his most important work consists



in collecting information regarding the trade and the commercial needs of his district, so that British traders may be able to open up or develop trade with that district. Some of these reports, which are issued by the Foreign Office in conjunction with the Commercial Department of the Board of Trade, are documents of great value and of interest to all who are engaged in commerce.

In business transactions, the Consul has the powers of a notary public and of a Commissioner for oaths. He is also empowered to impress documents with British stamp duty where necessary ; and any British subject who gets into difficulties—legal or otherwise—in a foreign country, may appeal to the nearest British Consul, when he may rely upon receiving such assistance as may be possible.

The principal trade document with which consuls and vice-consuls are concerned is known as the *Consular Invoice*. This is a special invoice form provided for the use of exporters. On the back is a declaration of accuracy which must be sworn to before the consul of the importing country, signed in his presence, and countersigned by him. This form is completed in triplicate, one copy being for the consul, one for the shippers, and one for the Customs authorities at the port of entry of the goods. The latter copy assists in the assessment of tariffs, and therefore facilitates clearance of the goods enumerated on it.

Exporters to Central and South American countries and to the United States must make a declaration before a local Consul to the effect that the information given in the consular invoice is a true and faithful description of the contents and value of the goods shipped. The invoices, signed by the exporter or his representative, is taken to the Consulate. A fee, varying according to the value of the goods and the country concerned, is charged by the Consul for legalising the invoice. This fee is known as *Consulage*, and is also charged by the Consul for the performance of certain other duties connected with his office.

**EXPORT CREDIT SCHEMES.**—Another development arising out of the war is the assistance that the Government gives to industry in times of great financial crises. This has taken the form of export credit for which the first provision was made in 1919. The finances and currencies of Europe were in a more chaotic state than the commercial men of that generation had ever known, and external



aid was required to facilitate the resumption of trade with countries whose commerce and industries had been crippled by the war. Under the original scheme advances were made to exporters whose trade with such countries would otherwise be at a standstill, but the foreign importers were required to find approved collateral security.

In 1921 this scheme was replaced by a system extended to all countries except Russia, and under which the payment of a proportion of bills of exchange was granted by the Exports Credit Department. Devised to meet still rather abnormal conditions of trade, the scheme was by no means simple, but it undoubtedly brought to this country a certain volume of business, which would otherwise have been placed elsewhere.

As the most important disturbances in international trade passed away a new scheme was instituted on the recommendation of a committee of bankers and others appointed in 1926 to examine the general question of credit insurance. The scheme came into force in 1929. The Exports Credit Guarantee Department insures payment at maturity of a proportion not greater than 75 per cent of bills of exchange drawn upon approved foreign importers in respect of goods manufactured in the United Kingdom. The greater part of the business of the Department is done under contracts or insurance policies designed to facilitate normal business in the principal exporting industries.

**ECONOMIC ADVISORY COUNCIL.**—This standing body, presided over by the Prime Minister, was introduced in 1930 to advise His Majesty's Government in economic matters. Its chief purpose is to make continuous study of developments in trade and industry and in the use of national and imperial resources, of the effect of legislation and fiscal policy at home and abroad, and of all aspects of national, imperial, and international economy with a bearing on the prosperity of the country. The Council may initiate inquiries into, and advise upon, any subject falling within its scope, including proposals for legislation. The reports and work of the Council are confidential unless it advises the Prime Minister otherwise.

**OTHER GOVERNMENT SERVICES.**—Other recent developments in the services rendered by the Government to the trader have been directed towards the encouragement of imperial trade and the making of the British Empire into a self-supporting unit.



The Imperial Shipping Committee, established in 1920, was the first body to be responsible to all the several Governments of the Empire, and was the organiser of a scheme of rebates similar to that which was practised early in the twentieth century by the shipping rings. Shippers who shipped exclusively by steamers belonging to the ring were granted a rebate of, say, 10 per cent on a year's freight. By this means freight rates were maintained and competition kept out. A system similar to this is organised by the Imperial Shipping Committee.

The Imperial Economic Committee was established in 1925 for the specific purpose of promoting imperial trade, if possible, with the help of some form of imperial preference. The Committee has presented reports on the marketing and preparation for the market of meat, dairy produce, fish, poultry, eggs and honey. It has also conducted inquiries into the possibilities of the Empire Tobacco industry and the Empire timber trade.

**Agricultural Marketing Boards.** These represent an attempt on the part of the State to plan the marketing of certain agricultural products with a view to eliminating the wide difference in price as between the producer and the consumer. The defects of the agricultural marketing system have been the subject of frequent comment by official committees of investigation. Thus, the Linlithgow Committee stated—

Farmers, for the most part, are men in a small way of business, and even when farming on a somewhat large scale the produce which they have individually to offer at any one time is an insignificant contribution to the total supply. Sales of such products as grain and livestock are intermittent and not of daily, or even weekly occurrence, so that the marketing side of their business, though of primary importance, takes a second place as compared with the more immediate problems of farm management.<sup>1</sup>

▷ In an attempt to place this side of agricultural activity upon a firmer basis, the *Agricultural Marketing Act*, 1931, was passed into law as an enabling measure. Under this Act it became possible for producers to mobilise themselves comprehensively for group action in the markets of this country. For this purpose the majority of the producers of a particular product could submit a scheme for regulating the marketing of it which, when approved by the Minister of Agriculture and by Parliament, became binding on the whole industry. It was, in fact, an Act to protect the main body of

<sup>1</sup> *Final Report of the Departmental Committee on Distribution and Prices of Agricultural Produce.*



producers against minorities who could otherwise wreck any policy which the industry might attempt to pursue in its common interest. This Act made no attempt to regulate imports so that the consumer was safeguarded from price exploitation by the possibility of outside competition. Again, there was no attempt to control production and no promise for assistance from the Treasury. Only one scheme was prepared under this Act alone, namely, for hops, a crop already protected by heavy import duties.

In 1933 a further Agricultural Marketing Act was introduced which gave power to regulate supplies, both of imports and of home grown produce. Hence it may be said that the machinery for formulating and operating schemes for the reorganisation of agricultural marketing is provided mainly by the 1931 Act, while the inducement to use it is in the Act of 1933. Under these Acts, any persons who satisfy the Minister of Agriculture that they are substantially representative of the producers of an agricultural product in a given area may submit a scheme for regulating the marketing of that produce in that area. The product may be either primary (such as beef, hides, eggs, or oats) or secondary (such as refined sugar, canned peas, bacon, or cheese). The scheme must provide for a register of producers of the regulated product, for a vote to be taken whether the scheme is to stay in force, for the constitution of a board elected to represent registered producers, for fines and arbitration in cases of dispute, for establishing a fund by contributions from producers, and for borrowing, lending, or guaranteeing money. Power may be taken under the Act for the board to buy, sell, advertise, transport, grade, or manufacture the regulated product, and to organise statistics, research, education, co-operation, or inspection in connection with it.

In addition to the Marketing Board itself various other bodies may be established. Thus a *Development Board* can be set up for each scheme with wide powers over the industry, including the reduction, suppression, or prevention of redundancy in productive capacity. Again, an important part in the experiment has to be played by *Agricultural Marketing Reorganisation Commissions*, each of which consists of a chairman and four other members appointed by the Minister. Their duties are to prepare marketing schemes which the Minister shall bring to the notice of the producers concerned, to investigate matters affecting any other schemes, or to



recommend measures to promote co-operation between marketing boards. The *Consumers' Committees*, of which there are three, represent the interests of consumers of all products regulated under the Acts. They are charged to report to the Minister upon complaints and upon the general effect of schemes in force upon the consumer. Reports from this and other sources may be referred to *Committees of Investigation*, which call for explanations and report to the Minister, who may as a result revoke or amend the scheme. There is also a *Markets Supply Committee* to review the annual supply of agricultural products in the United Kingdom and to advise on import questions; and three *Market Facilities Committees* to make and renew loans out of agricultural marketing funds.

Marketing schemes have been introduced in respect of hops, milk, pigs, bacon, and potatoes, whilst others are in contemplation. Considerable difficulties have been encountered in connection with the administration of the schemes on account of the fact that the whole structure is new, and as yet imperfectly modelled. Consequently criticism of the schemes comes from producers, distributors, and consumers alike, and there is little doubt that revision of them will be necessary in the near future.

### TEST PAPER LXX

1. Account for the origin of the Consular Service.
2. Enumerate some of the chief duties of a Consul.
3. What services do Consuls render to Commerce?
4. What is meant by a consular invoice?
5. What attempts have been made by the Government to render financial assistance to traders in times of crises?
6. What are the chief methods of promoting trade adopted by (a) the Imperial Shipping Committee, and (b) the Imperial Economic Committee?
7. In the case of a certain export (invoice value of goods being £1,000) under the Export Credits Scheme the Department of Overseas Trade guaranteed 100 per cent of the total amount of the bill drawn against the shipment. The foreign importer lodged with the Department security estimated to cover half the amount, the Department retaining recourse against the exporter for 57½ per cent of any loss incurred. At the end of twelve months the importer paid £85, and at the end of a further three months the security lodged was sold and realised £525. Find the total loss incurred and the share of it borne by the exporter, interest having been charged on all outstanding sums at the rate of 5 per cent per annum.
8. Explain briefly the functions of the Agricultural Marketing Boards.



## CHAPTER LXXI

### THE POST OFFICE

TO-DAY, all civilised communities have a well organised postal system. The term "post office," however, is usually applied to the building where postal business is transacted, and in Great Britain it is used for the General Post Office in London, and also to district offices and small branch offices. In remote country districts the post office is often run in conjunction with a general stores.

**HISTORICAL DEVELOPMENT.**—The real beginning of the Post Office dates from the year 1512, when Sir Brian Tuke was appointed the first Master of the Post. His duty was to look after the relays of post horses maintained on the regular post roads at the King's expense. The first serious attempt to establish a monopoly for the Royal posts is contained in a proclamation of Queen Elizabeth in 1591.

A scale of postal rates, graduated by distance to cover the costs of relays of post horses, was introduced about the year 1635, when the Central Post Office was established in the City of London. In 1784 a mail coach service was organised, and for the next fifty years constituted the chief means of transport for postal matter; ultimately, it was forestalled by the railway. In 1812 the postal rate for a single sheet letter from London to Liverpool had risen to eleven pence. Rowland Hill reformed this system, and in 1840 the Penny Post was adopted, the charge being governed by weight instead of by distance. In 1874 the International Postal Union established a uniform rate of 2½d. per ounce for letters to Europe; in 1898 the Imperial Penny Post was inaugurated, and subsequently extended to the United States. As a result of the War the rates of postage have been temporarily increased.

**FUNCTIONS OF THE POST OFFICE.**—The Post Office is a government department under the control of the Postmaster-General with the aid of an Assistant Postmaster-General and a staff of permanent officials. The activities of the Post Office are both numerous and varied, and students should consult the official *Post Office Guide* for a full account of its manifold services. An attempt has been made



to classify its main functions in the table on pages 850 and 851, from which it will be seen that its activities may be grouped under the following headings—

- (1) Carrier or Postal Services.
- (2) Banking Services.
- (3) Insurance Services.
- (4) Means of Communication.
- (5) Agent for the Government.

(1) **The Post Office as a Carrier.** The conveyance of mails was the original function of the Post Office, and the postal service still remains the most important of its now very numerous activities. The matter carried consists of ordinary letters, registered letters, samples, newspapers, and printed papers for delivery both at home and abroad. More people are employed on these services than on all the other Post Office departments put together. Letters and packages have to be posted, collected, forwarded, and delivered, and the problem of the Post Office is to effect these operations as quickly and as economically as modern invention will allow. Mechanical and electrical aids have become an established feature, and the introduction of shutes, conveyor bands, lifts, and other electrical appliances has done much towards reducing the time taken for the handling of correspondence, and has minimised the labour involved in dealing with parcels and mail bags.

An innovation of 1926 was the establishment of the *Cash-on-Delivery Service*. By this service tradesmen and others may send parcels, and the price will be collected from the addressees and remitted to the sender by the Post Office. A small charge in addition to the usual postage is made, and must be prepaid by the sender. This service is much utilised by the large mail-order firms. The *sample post* is another useful service to merchants and manufacturers, since it enables them to dispatch at a cheap rate *bona fide* trade samples without saleable value.

The *Business Reply Service*, introduced in 1932, was designed to reduce the expense incurred by business houses in enclosing stamped addressed cards or envelopes, many of which were not used for the desired purpose. The sender, under licence from the Post Office, may enclose with his communication a specially printed addressed card or envelope which the client may post in the usual way, but



unstamped. The following is an example of a Business Reply Card—

### FRONT SIDE OF CARD

<b>Postage will be paid by Park Coal Co., (Cardiff) Ltd.</b>	<div style="border: 1px solid black; padding: 5px; margin: 0 auto; width: 80%;"> <b>BUSINESS REPLY CARD</b>            Licence No. 1747         </div>	<b>No Postage Stamp necessary if posted in Great Britain or Northern Ireland.</b>
Date .....10th Feb.....19 ... Please deliver ..... Five..... Tons of ..... M.D. LARGE @ 41/- per ton on.... Monday ... next. Name .....W. J. Martin, ..... Address .....35 High St., Cardiff...		<b>PARK COAL CO. (Cardiff) Ltd., Salisbury Road, Cardiff.</b>

### REVERSE SIDE OF CARD

<b>PARK COAL CO. (CARDIFF) LTD.</b> SALISBURY ROAD. Telephone No. 3098	
<b>CURRENT PRICE LIST</b> January 1st, 19..	
<b>GUARANTEED MAESTEG DEEP COALS</b> The Coal with the Certificate	
	<i>Per ton</i>
M.D. LARGE.....	41/-
M.D. COBBLES.....3 to 5 inches .....	38/6
M.D. NUTS .....1 to 3 inches .....	33/6
M.D. Rubbly Small .....1s. 6d. per cwt. ....	30/-
<b>SIZED ANTHRACITE</b>	
Anthracite Cobbles .....	42/6
Best Anthracite Stove Nuts.....1-1½ .....	63/-
Anthracite Pea Nuts .....¾-1½ .....	45/6
Anthracite Peas .....¾-¾ .....	40/-
Anthracite Grains .....¾-¾ .....	35/-
Above prices are less 1s. per ton for cash within 14 days.	



The Post Office debits the licensee with the postage due plus a half-penny fee in each case. A similar system is also available for parcels and telegrams.

Perhaps the most recent innovation is the *Raillex* Service, which came into operation in 1934. It is intended to secure the transmission of a letter not exceeding 2 oz. in weight as rapidly as transport facilities will allow and with a minimum of trouble to the sender. The Post Office, for an inclusive fee of 2s. 6d., accepts a Raillex letter at a Post Office and forwards it by special messenger to the railway station for dispatch by the first suitable train, informing the Post Office express delivery office nearest the station of destination of the dispatch of the letter. A messenger awaits its arrival and delivers it immediately by the quickest possible means to the addressee. This should constitute a useful emergency service.

Since 1934 there has been established a system of inland air mail lines between London and a number of the greater cities, such as Birmingham, Manchester, Liverpool, Belfast, the Isle of Man, Glasgow, Bristol, Cardiff, Plymouth, and Southampton. Letters weighing not more than 2 oz. are carried without extra charge, but over 2 oz. the rate is 1d. per oz. There is also a regular weekly air mail service to Australia.

(2) **The Post Office as a Banker.** The Post Office acts as a banker in two ways—as an agency for the remittance of money and as an agency for saving an investment.

It acts as an agency for the remittance of money through its system of postal orders and money orders. These are chiefly valuable where small sums are concerned. The cash-on-delivery parcel service supplements the money-order service proper, and these, together with more exceptional facilities, such as telegraph money orders, offer the public a useful range of services at low rates of commission.

The Post Office Savings Bank may claim to be an important instrument both of prudent national saving and wise national spending. It is the bank of the people, and there is a branch in every city and town, and in almost every village in the country. Closely allied to the Savings Bank is the work of issuing and repaying *National Savings Certificates*. This scheme originated as a temporary expedient during the War, but it has now become a national institution. The Post Office undertook the sale of the certificates and



custody of the records from the start. Unlike a Savings Bank deposit, a savings certificate is normally a long term deposit, and savings certificates are essentially investments and not savings for use at a relatively early date. They constitute a means of investing at a satisfactory rate of interest, free of income tax.

The Savings Bank also maintains a register of Government stock and offers facilities to the small investor, particularly in connection with Savings Bank deposit accounts, for purchasing and selling these securities at a reasonable rate of commission. The facilities are, of course, not intended for the type of client who would normally transact business through a stockbroker.

(3) **The Post Office as an Insurer.** As an insurer the Post Office registers or insures letters and parcels for a small fee and also deals in life assurance annuities. In the *Registered Letter Service* an extra fee is charged over and above the ordinary postage. For foreign letters there is a further service, called the *Insurance Letter Service*, under which a letter may be insured for the declared value up to certain limits by payment of an extra fee. The maximum amount of compensation obtainable is £400 on payment of an extra fee, over and above the postage, of 1s. 11d.

Depositors in the Post Office Savings Bank may purchase annuities on their own lives or the lives of any person over 5 years of age, for any sum from £1 to £300 per annum. Annuities are payable in equal quarterly instalments. Thus, under this system a depositor may make provision for himself and family all under the guarantee of Government.

The Post Office is also entrusted with the sale of National Health Insurance and Unemployment Insurance Stamps. In connection with these it also issues the necessary cards to which the stamps are affixed.

(4) **The Post Office as a Means of Communication.** In the transmission of intelligence the Post Office acts as a means of communication. For this purpose it utilises the telegraph and the telephone, of which it has a monopoly of all routes in Great Britain, and all principal Post Offices are telegraph offices. Within recent years rapid and revolutionary changes have been made in these services, and it can be stated with confidence that they are both efficiently and economically run.

**THE TELEGRAPH.** Telegraphic communication plays an important



part in the business of the world, and the extension of cables to the utmost parts of the earth has largely tended to prevent sudden and disastrous variations in the prices of the various commodities which form the staples of Commerce. For example, the movements of the Cotton Market at Liverpool are known as soon in New Orleans and other American cities, and in Egypt and India, as they are in other parts of England. No sooner does a rise in the price of this important raw material occur in Liverpool, than merchants in America and elsewhere make arrangements to increase their shipments so that they may participate in the profits resulting from the increased prices.

The knowledge of this in Liverpool reacts upon the market, and any attempt to force up the price of the cotton unduly is frustrated.

Like many other things, the rapid communication of news and commercial intelligence has been transformed from a luxury into an everyday necessity, and commerce without the electric telegraph would be paralysed. Inland telegrams, which means telegrams between all parts of the British Isles, are charged for at a fixed rate for the first twelve words (or less), and an extra charge is made for each additional word—the postage stamps to be affixed to the form by the sender. Five figures count as one word; and where a letter precedes or follows a group of figures, it is counted as a separate word. The address of the receiver is charged for, and also that of the sender, except when written on the back of the telegraph form, in which case it is “for reference only.” For ordinary inland telegrams, plain language rendered as briefly as possible is used.

*Foreign Telegrams* may be written in plain or in secret language. For the latter purpose, several more or less ingenious works, called “Codes,” have been invented, and are in general use; whilst some firms with foreign branches have private codes of their own. The object of using a code is to reduce the cost of telegraphing, since a single word may be made to represent a whole sentence; and this is an important consideration, when it is remembered that a single word often costs several shillings. International telegraph rules provide that in code language ten letters shall be the maximum allowed in one word or group, as against fifteen in plain language. In cypher five is the maximum allowed in a group, and letters only or figures only can be used. The code may be a



published one or a private one for use only between the owner of the code and his correspondents, and constructed to serve the owner's own particular needs. The published codes are arranged to suit various trades, and by means of them information of every possible description may be wired.

*The Use of a Code.* The best known work of this kind is the A B C Code. This contains 100,564 words, alphabetically arranged and numbered so that each word also represents a certain number. Each word or number indicates a complete sentence, which anyone in the possession of the book can decipher. The sentences which correspond to these words are arranged according to subject-matter. For example, one section refers to the acceptance of bills, another to insurance, another to the time and conditions of delivery ; further, for every quantity in English or Metric weight and measures, there is a code word, as well as for the price in English money, in dollars, in marks, and in francs. If a person desires to send a telegram, he turns to the alphabetical arrangement of the sentences and their contents, notes the corresponding code word, and thus puts together the telegram. The receiver, on the other hand, refers to the alphabetical arrangement of the code-words and reads off the equivalent sentence.

An example will make this clear—

A, in London, desires to cable the following to New York—

(a) *There is an unfavourable change of market.*

He looks in the code under the word "market" and finds the required sentence with the code-word—

No. 25820 = "Malchance."

(b) *Do not commence packing until you have further instructions.*

Under the heading of "packing," the following code-word is given for this sentence—

No. 29380 = "Paddock."

(c) *What is the smallest quantity you can send ?*

He looks under the heading "quantity" and finds the following code-word for this sentence—

No. 32178 = "Queatur."

Assuming that the firms A and B have agreed to use the A B C



Code in their cable correspondence, A writes out the following telegram—

“ B. New York  
Malchance Paddock Queatur.”

He could also cable 25820, 29380, 32178, as already mentioned ; but since mistakes are more likely to occur with the use of figures, the words are usually preferred.

B, the receiver of the cablegram in New York, looks up the three words in the A B C Code and finds the three sentences ; instead of twenty-five words having to be used, the message has been dispatched by the use of three.

*Secret Codes.* Between banks and their branches and agencies, and in cases where absolute secrecy is required, cypher codes are used, which are composed wholly, or in part, of figures having a secret meaning. Every separate figure is charged as one word, and every group of five figures is charged as a word, larger groups being counted at the rate of five figures to a word, one word being added for any excess. Messages by these cypher codes can only be interpreted by the holders of the key. All communications between Governments and their representatives abroad are, when “ wired,” written in cypher.

The Post Office has the monopoly of all telegraph routes in the British Isles, including the Channel Islands, and most post offices are now telegraph offices. In London, cable messages are received at, and delivered from, the offices of the various companies owning the cables. In the provinces, these messages are usually taken in at the postal telegraph offices and transmitted by the inland lines either to London or to the point on the coast at which the cable company's system commences.

THE TELEPHONE. In the case of local telephone calls the caller pays for the service by placing two pennies in the special coin box affixed to the call office. With trunk calls the caller usually passes his call to the clerk at the telegraph counter ; after collecting the appropriate charge this person then puts the call through the trunk exchange. When the call matures the exchange notifies the telegraph counter clerk, who informs the waiting caller to which box his call will be switched. To this branch of work a number of other services are attached, such as telephoning express letters to other



## MAIN FUNCTIONS OF

<p><b>I. Carrier Services.</b></p>	<p>The collection, carriage and delivery of correspondence and small parcels.</p>	<p><b>INLAND CORRESPONDENCE</b> includes matter addressed to places within Great Britain and Northern Ireland. It is divided into five classes: (a) Letters; (b) Post Cards; (c) Printed Papers; (d) Newspapers; (e) Parcels. Letter Rates: Not exceeding 2 oz. 2½d. For each additional 2 oz. or part thereof ½d.</p> <p><b>COLONIAL CORRESPONDENCE</b> includes all countries within the British Empire, except Iraq and Transjordan, and the United States of America and Egypt. Letter Rates: Not exceeding 1 oz. 2½d. For each additional oz. or part thereof 1d.</p> <p><b>FOREIGN CORRESPONDENCE</b> embraces all countries not included in the above. Letter rates: Not exceeding 1 oz. 3d. For each additional oz. or part thereof 1½d.</p> <p>Other postal services include—</p> <ul style="list-style-type: none"> <li>(i) Late Fee Letters.</li> <li>(ii) Express Delivery.</li> <li>(iii) Railway Letters.</li> <li>(iv) Private Boxes and Bags.</li> <li>(v) Poste Restante.</li> </ul>
<p><b>II. Banking Services.</b></p>	<p>Agency for the remittance of money.</p>	<p>The Post Office undertakes the functions of a banking organization in its remittance business, the postal order and money order services. These are chiefly valuable where small sums are concerned.</p> <p><b>MONEY ORDERS</b> are made by one post office upon another <u>specified</u> post office for the payment on demand to a named person a certain specified sum not exceeding £40.</p> <p><b>POSTAL ORDERS</b> are made by one post office upon <u>any</u> other post office for the payment upon demand to a named person of a specified sum not exceeding £1 1s. (plus 5d. in affixed stamps).</p>
	<p>Agency for saving and investment.</p>	<p><b>SAVINGS BANK.</b> The Post Office acts as a savings bank throughout Great Britain and Northern Ireland. Deposits may be made in every town and almost every village. The system was inaugurated in 1861 with the object of providing a safe, simple, and readily accessible means of deposit for the savings of the public.</p> <p><b>NATIONAL SAVINGS CERTIFICATES.</b> Closely allied to the savings bank business is the work of issuing and repaying National Savings Certificates. This scheme originated as a temporary expedient during the War, but it has now become a national institution.</p> <p><b>GOVERNMENT SECURITIES.</b> The savings bank arranges for investments by depositors in Government Stock and offers facilities to the small investor for purchasing and selling these securities at a reasonable rate of commission.</p>



## THE POST OFFICE

<p>III. Insurance Services.</p>	<p>Safeguarding life and property against loss and other contingencies.</p>	<p><b>REGISTERED PACKETS.</b> The Post Office agrees to pay compensation up to a limit of £400 for the non-delivery of inland registered packets containing bank notes, cheques, postal orders, and money orders. It also effects insurance of foreign and colonial packets, and also sells insurance stamps.</p> <p><b>LIFE ANNUITIES.</b> Savings bank depositors may purchase annuities on their own lives or the lives of any person over 5 years of age for any sum from £1 to £300 per annum.</p> <p><b>NATIONAL INSURANCE.</b> In connection with National Insurance Schemes the machinery of the Post Office makes collection of contributions practicable by its sale of Health and Pensions, and Unemployment Insurance Stamps of various denominations, and assists in the administration of the Insurance Acts by issuing contribution and emergency cards.</p>
<p>IV. Means of Communication</p>	<p>The transmission of intelligence.</p>	<p><b>TELEGRAPH.</b> The inland telegram is the most suitable means for the rapid transmission of a written message. Messages may be sent abroad by cable or wireless.</p> <p>The telegraph service has experienced great changes within recent times, for the methods of telegraphy have been completely altered. Morse working has practically disappeared in favour of the now ubiquitous teleprinter, an instrument with a keyboard similar to that of a typewriter.</p> <p><b>TELEPHONE.</b> This system embraces two sections: (1) Local or Short Distance lines, and (2) Trunk or Long Distance lines. Calls can now be made to most countries of Europe and to many places over-seas.</p>
<p>V. Agent for the Government.</p>	<p>Miscellaneous Services.</p>	<p><b>SOCIAL SERVICES.</b> The use made of Post Office machinery by departments responsible for the administration of social services has shown heavy expansion in the last decade.</p> <p><b>OLD AGE PENSIONS.</b> The Post Office pays widows', orphans', and old age pensions, and naval, military, and air force pensions and allowances, on behalf of the issuing authorities.</p> <p><b>LICENCES.</b> In addition to the sale of wireless licences, the Post Office is concerned with the sale of many types of licence on behalf of the Licensing Authorities concerned. The most familiar to the public are the dog licence and the motor vehicle renewal licence. The list includes also armorial bearings, male servants, game, gun, and hounds licences.</p>



towns for delivery by a special messenger. The charges in this case include the usual trunk call fee plus a mileage fee for delivery at the other end. This charge must be paid by the person originating the call.

(5) **The Post Office as an Agent for the Government.** As an agent for the Government, the Post Office issues Inland Revenue Licences and provides for the payment of Old Age Pensions, Ex Army and Navy disability pensions, and next of kin pensions for those who fell in the Great War. It should be noted that only *renewals* of Motor Vehicle Licences are issued by the Post Office, the original licence being taken out through the local government authority of the area in which the licence is desired. In the case of other licences, both the original issue and the renewal are effected through the Post Office. It also assists other Government Departments by the sale of stamps in payment, for instance, of the Entertainment Duty and also of the Income Tax. Indeed, one of the most striking developments of Post Office activities within recent times has been its gradual assumption of functions which have no connection whatever with its primary purpose, but which have been imposed upon it because its far-reaching organisation has presented the only means of carrying out with reasonable economy certain social services which the State has from time to time thought fit to establish.

### TEST PAPER LXXI

1. Describe briefly the main functions of the Post Office?
2. What influence have the telegraph and the cable had upon the organisation of the market?
3. Messrs. Thomas Holt & Co., of 128 Market Street, Manchester (Telegrams: "Holt, Manchester"), have just received 10 bags of Granulated Sugar ordered from Messrs. Joseph Taverner & Son, of 119 Great Cobalt Street, London (Telegrams: "Grano, London"). Messrs. Holt find that five of the bags have been seriously damaged by sea-water. Draft, in as few words as possible, a telegram from Messrs. Holt explaining the matter and, at the same time, ordering another five bags to be dispatched at once.
4. What methods are adopted by merchants to reduce the cost of telegraphing to places abroad?
5. What is a cable word?
6. "Telegraphic codes may be called the 'shorthand' of telegraphic communication." Explain this statement.
7. Write a full note on the telegraphic system as applied to commerce, both inland and foreign. State what you know about "codes." Name two important ones, and explain how a secret code may be made between an exporter in this country and his agent in Melbourne.



## CHAPTER LXXII

### THE INCOME TAX

**NATURE OF TAXATION.**—A tax is a “compulsory contribution of the wealth of a person or body of persons, for the service of the public powers” (*Bastable*). The following points should be noted—

(1) A tax is *compulsory*. There are those who think that the income of the State might be derived from voluntary contributions. The whole theory of taxation, however, depends upon the fact that taxes are compulsory.

(2) A tax is a *contribution*. It is a deduction from the wealth of the payer and is used for the maintenance of the State.

(3) The contribution must consist of *wealth*, i.e. something of value which is the result of production.

(4) The tax is paid by a *person* and is always a deduction from his wealth. It is always a person who is taxed and never a thing.

(5) A tax is for the *service of the public powers*. The services which are performed by the public powers have to be paid for, and the taxes are used to meet these payments.

**CANONS OF TAXATION.**—The following principles were enunciated by Adam Smith—

(1) **Equality.** “The subjects of every State ought to contribute towards the support of the Government as nearly as possible in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the State.”

(2) **Certainty.** “The tax which each individual is bound to pay ought to be certain and not arbitrary. The time of payment, the manner of payment, and the quantity to be paid, ought to be clear and plain to the contributor and to every other person.”

(3) **Convenience.** “Every tax ought to be levied at the time, or in the manner in which it is most likely to be convenient for the contributor to pay it.”

(4) **Economy.** “Every tax ought to be so contrived as both to take out and keep out of the pockets of the people as little as possible over and above what it brings into the public treasury of the State.”

**THE INCOME TAX.**—The income tax of the United Kingdom



yields the largest amount of revenue of any single tax in the British system. It was first introduced in 1799 and remained in force until 1816. It was reintroduced in 1842 broadly upon the same lines, and has continued in existence ever since. Income tax is, therefore, in substance a permanent tax, but it is in fact reimposed annually by way of the Finance Act for a period of one year only.

The laws relating to income tax were consolidated by the Income Tax Act, 1918, and the income tax is now levied under a code consisting of that Act and subsequent amending legislation. A Committee appointed by the Government is at present engaged in codifying the Income Tax Acts. The aim is to make the income tax law as intelligible to the taxpayer as the nature of the legislation admits, and, to this end, the Committee is to suggest any alterations which would promote uniformity and simplicity, while leaving substantially unaffected the liability of the taxpayer, the general system of administration, and the powers and duties of the various authorities concerned therein.

**Method of Charge.** Income tax is levied only on (a) income arising within the United Kingdom, irrespective of the nationality or the place of residence of the beneficial owner, and (b) income from abroad belonging to any person residing in the United Kingdom.

For the purposes of assessment, all chargeable income is classified according to source into five groups, or "Schedules."

*Schedule A* deals with income from the ownership of land, buildings or houses in the United Kingdom.

*Schedule B* deals with income from the occupation of land in the United Kingdom.

*Schedule C* deals with income arising from British, Dominion, or Foreign Government Securities.

*Schedule D* deals with—

(a) Profits from trades, professions, and vocations carried on in the United Kingdom.

(b) Interest, dividends, and other annual payments.

(c) Income from abroad (except that charged under Schedule C).

(d) Income derived from any source not included in this or other Schedules.

*Schedule E* deals with income from offices and employments.

Income tax is assessed each year for the "year of assessment" commencing on 6th April, and falls into two parts: that charged at a



# COMPARISON OF CERTAIN TAXES IN THE LIGHT OF ADAM SMITH'S CANONS OF TAXATION

Tax	Equality	Certainty	Convenience	Economy
Income Tax.	This tax is one of the most equitable devised. The system of exemptions and rebates relieves the poorer classes.	Calculation of the tax is often complicated so that this canon is often infringed.	The time of collection is known to the payer.	In general it may be said that the tax is economical to collect.
Customs Duties.	They press more heavily on the poorer classes than on the rich, e.g. duties on tobacco.	The tax is certain and easy to calculate.	Goods may be stored in bond, and payment made when convenient.	Collection is fairly economical, though an elaborate supervision of imports is necessary.
Estate Duties.	They are graduated so as to press most heavily on the wealthy.	The amounts which are levied are certain and may be calculated with little difficulty.	The tax is levied when estate passes so that the time may be said to be convenient for payment.	They are economical to collect.
Stamp Duties.	Certain of these are graduated on an ad valorem basis, but others (e.g. receipt stamps) are very unequal in their incidence.	The taxes are easily assessed.	They are paid at a convenient time when sums of money are being transferred.	They are easily collected.



standard rate, and that charged at higher rates. The former applies generally, the latter only to individuals with large incomes. In practice only the former is referred to as the income tax, and the latter is referred to as the sur-tax. A sur-tax payer is a person whose income exceeds £1,500. The sur-tax is administered under that name separately from the income tax, and it is more convenient to look upon it as though it were a separate tax. But in law both the income tax and the sur-tax form part of one tax, and indeed the sur-tax of an individual for any year represents, in strictness, the difference between the total tax payable by him and the tax chargeable at the standard rate.

**Differentiation and Graduation of Income.** In the case of individuals resident in the United Kingdom, discrimination is made between income earned by personal exertion and income not so earned. This is effected by giving an allowance at the standard rate on an amount equal to one-tenth of the earned income, up to a maximum allowance of tax on £150. The allowance is not given to non-residents or to companies.

Companies are liable in all cases to income tax at the standard rate and, save in exceptional circumstances, are not liable to sur-tax.

**Taxation at the Source.** A special characteristic of the British Income Tax is that, wherever possible, tax is assessed upon and collected from the person through whose hands the income passes before it reaches the actual owner. The first receiver is entitled by law to recover the amount of tax paid by making a deduction from the income before passing it on to the owner. As an example, consider the case of a house let to a tenant. Although the tax on the income arising from the ownership of the property (i.e. the rent) is ultimately borne by the landlord, the person assessed is the tenant who is bound to pay the tax charged. When paying the rent, the tenant deducts therefrom the tax paid by him. In the same way, the landlord is entitled to deduct from any payment of ground rent, or mortgage interest secured on the property the amount of tax appropriate to such payment, since this tax has already been paid to the Inland Revenue by the tenant. Thus, by means of one assessment, Income Tax is collected from the landlord of the house, the ground landlord, and the mortgagee.

Again, a limited liability company carrying on a trade is assessed and pays tax upon the whole profits it makes, without regard to the



manner in which those profits are distributed. Dividends and debenture interest are paid less the amount of tax appropriate thereto, so that the tax payable by the shareholders and debenture-holders is collected through the company.

The advantage of the system is that it greatly reduces the number of assessments necessary, and limits the possibility of evasion. The principal disadvantage is that it gives rise to a large number of repayment claims by persons entitled to relief.

The same principle is now being adopted by certain employers with regard to the remuneration paid to their employees. The amount of tax payable by each employee is agreed with the Inland Revenue Department, and the total is paid by the employer, who recovers this by deduction from the employees' salaries. This system is applied to salaries and pensions paid to Government and railway officials under the provisions of the Income Tax Act, and was in 1940 applied generally to the collection of tax payable under Schedule E.

**Personal Reliefs.** A person whose net statutory income does not exceed £110 is entitled to total exemption from tax. Provision is made for a marginal relief in cases where the total income is greater than £110, but less than £133. In these cases, the tax payable is not to exceed three-quarters of the excess of the total income above £110. In order to graduate the amount of tax payable according to the financial position of the individual, certain personal allowances are granted varying with the circumstances of each taxpayer. The reliefs are not granted to an individual who is not resident in the United Kingdom unless he is a British subject or resides in the Isle of Man, or the Channel Islands, and then only to the extent of the ratio between his British income and his total income.

(a) *Earned Income Allowance.* The Act provides that income earned as a result of personal effort should be relieved from tax to a greater extent than any other kind of income ("investment" income). A deduction of one-tenth from the net amount of any earned income is therefore allowed, subject to a maximum allowance of £150.

(b) *Age Allowance.* A similar allowance is granted in respect of investment income where a taxpayer (or his wife) was at the beginning of the year of assessment 65 years of age or more, and whose total statutory income does not exceed £500. As the tax



payable by an individual whose income slightly exceeds £500 might be disproportionately large compared to that payable if the income were slightly under this figure, a "marginal" relief is granted, so that the tax shall not exceed—

(1) The tax which would have been payable if the income was exactly £500, plus

(2) three-quarters of the amount by which the income exceeds £500.

(c) *Personal Allowance.* The personal allowance is £140 in the case of a man who has a wife living with him or whose wife is maintained by him by means of an allowance from which he is not entitled to deduct tax, and £80 in all other cases.

Where the £140 allowance is made, and the wife has any earned income of her own, an additional allowance is made equal to nine-tenths of the wife's earned income, subject to a maximum allowance of the tax on £45.

(d) *Housekeeper Allowance.* This allowance, which amounts to £50, may be claimed by—

(1) A widower, or widow, who has a female person resident with him or her to look after his or her children, or to act as housekeeper.

(2) An unmarried person who maintains a female relative resident with him to look after his younger brothers or sisters in respect of whom he has been granted child allowance.

(e) *Child Allowance.* Any person who has a child or children (including adopted children and step-children) under sixteen years of age is entitled to an allowance of £50 for each child. The allowance is also granted if the children are over sixteen years of age, but are receiving full-time education at a recognised educational establishment or an apprentice for a period of at least two years, when the emoluments do not exceed £13 per annum.

It is not essential that the person should be maintaining the child, or having the custody of it (except in the case of an adopted child). No deduction can, however, be allowed if the child's income exceeds £50, excluding income from any scholarship.

(f) *Dependent Relatives.* An individual is granted an allowance of £25 if—

(1) He maintains a relative of himself or his wife, and



(2) the relative, except a widowed mother, is incapacitated by old age or infirmity from maintaining himself, and

(3) the relative's income does not exceed £50 per annum.

If more than one individual contributes to the maintenance of the relative, the allowance is divided proportionately between them. A similar allowance is given to an individual who maintains a daughter living with him on account of his old age or infirmity.

(g) *Rate Chargeable.* For the year 1941-2 the standard rate is 10s., but the first £165 of taxable income is charged at only 6s. 6d. in the £.

(h) *Life Assurance Relief.* Relief is granted in respect of premiums paid during the year of assessment by an individual or his wife for an insurance or an annuity on the life of either. So much of the premium on any particular life policy as exceeds 7 per cent of the sum assured at death does not rank as allowance.

Where there is no sum assured at death, as in the case of an annuity, only policies or contracts effected on or before 22nd June, 1916, are taken into consideration, and then only to the extent of £100 of premiums in the aggregate for all such policies.

After these adjustments, the total premiums are subject to a further restriction of one-sixth of the total income of the individual.

The allowance is then made by means of a deduction of tax, calculated at the following rates—

(1) Where the contract was effected on or before 22nd June, 1916—

(a) Where the total income does not exceed £1000, at 3s. 6d. in the £.

(b) At 5s. 3d. if the net statutory income is greater than £1000, but less than £2000.

(c) At 7s. 0d. if the net statutory income exceeds £2000.

(2) Where the policy or contract was effected after 22nd June, 1916—

At 3s. 6d. in the £.

**Returns of Income.** Every person chargeable to Income Tax must, when called upon to do so, make and deliver to the authorities a return of his total income. The return forms are normally issued in April, i.e. at the beginning of the year of assessment. The taxpayer is naturally unable to estimate accurately what his income will be for a year which has only just commenced, but assessments on untaxed income are normally based upon the amount of income arising in the year preceding the year of assessment. In a return,



therefore, for the year 1939/40, the taxpayer is required to state his total income for the year 1938/39, ended 5th April, 1939. He is also required to notify any changes in the sources of his income that took place during that year. A section is also included in the form to enable the taxpayer to claim his personal reliefs.

**Statutory Total Income.** The total income shown on an individual's return has no relation to his statutory total income, either for the year of assessment, or for the preceding year. The statutory total income for any year of assessment is arrived at as follows—

- (a) All assessments for the year upon untaxed income and property, plus
- (b) all taxed income received during the year of assessment, minus
- (c) all charges payable during the year of assessment (i.e. annual payments from which Income Tax may be deducted, as explained on page 856).

**Determination of Assessable Profit.** The Income Tax Acts provide that profits assessable under Schedule D shall be computed for Income Tax purposes in accordance with ordinary commercial principles, subject to certain specific directions affecting the allowance of expenses. Thus, an expense is allowable as an Income Tax deduction only if it is wholly and exclusively incurred in earning the profit, and is not of a capital nature. The actual amount of the assessment, therefore, is rarely the amount which the proprietor would consider to have been earned.

The following expenses are not allowable as deductions in computing the assessable profits—

- (1) Sums charged for drawings by proprietors, partners' salaries, or interest on capital.
- (2) Annuities, royalties, and annual interest generally. (Tax on such amounts should be deducted before payment is made.)
- (3) Sums paid as Income Tax under any Schedule.
- (4) Sums expended in improvement of premises, or written off for depreciation of land, buildings, or leases.
- (5) Losses not connected with, or arising out of the business.
- (6) Wear and tear of machinery and plant. A deduction from the assessment, may, however, be claimed under this heading.

The following expenses are allowable as deductions—

- (1) Sums expended on repairs to the business premises.



(2) Bad debts, and doubtful debts, to the extent that they are estimated to be bad.

(3) Rent of business premises. If part of the premises is used as a residence, only the appropriate proportion of the rent is allowable.

(4) Obsolescence of plant and machinery. When obsolete machinery is replaced, an allowance may be claimed equal to the written-down value, less any sum realised by its sale. The written-down value is calculated by deducting from the original cost of the machinery the total allowance granted in respect of wear and tear.

The amount of the Income Tax assessment is therefore computed by adding any expenses disallowed to the actual amount of the trading profit.

**POST-WAR CREDIT.**—In 1939 and 1940, there was much discussion of a proposal put forward by Mr. J. M. Keynes for what was first described as “compulsory saving,” and later, as “deferred pay.” The object of the scheme was to deprive the individual of purchasing power which, if used by him, would cause an inflationary rise in prices. A compulsory deduction from income was therefore suggested, the amount of the deduction varying with the size of the income and with the family and other obligations of the individual. The sum thus deducted would be credited to the individual and would be made available to him at the end of the war. The same result could, of course, have been achieved by the imposition of additional taxes, but it was felt that if taxes were increased beyond a certain limit, the psychological effects upon taxpayers might prove injurious to the war effort.

The substance of the plan was adopted in the 1941 Budget which increased the burden of the income tax, not merely by raising the standard rate of tax, but also by drastic adjustments of personal allowances. This had the effect of creating about three million new taxpayers whose incomes had hitherto been small enough to be completely exempt. It was provided in Section 7 of the Finance Act, 1941, that the additional tax which an individual might bear for the year 1941–42 or any subsequent war year, by reason of the reductions made by that Act in the earned income allowance, the age allowance, the personal allowance and the exemption limit, is to be recorded year by year and credited to the individual in the Post Office Savings Bank as soon as possible after the termination of hostilities.



The subject of Income Tax is so wide and complex that any attempt to deal exhaustively with it is quite beyond the scope of this treatise. For further details relating to the various Acts, the student is recommended to read some standard work upon the subject, and also to consult the Finance Act of the current year, for information as to prevailing rates of tax.

### TEST PAPER LXXII

1. Explain the object of the Income Tax.
2. Name the various schedules and describe the purpose of each.
3. State carefully what is meant by "Taxation at the source." Illustrate your answer by reference to the schedules of Income Tax.
4. Enumerate some of the deductions which the merchant is allowed to make from gross profits in the preparation of his Income Tax return.
5. Give five items which are not allowed to be deducted from profits when preparing the Income Tax return.



## CHAPTER LXXIII

### BANKRUPTCY AND LIQUIDATION

It sometimes happens that a business man will find himself unable to pay all his creditors in full and his estate will have to be administered under the insolvency laws, so that his creditors may be paid as much as possible after the realisation of the assets. It does not necessarily follow that the debtor will be a bankrupt, as, for example, the realisation and distribution may take place under a *Deed of Arrangement*, but it is possible for the estate to be dealt with under the Bankruptcy Acts. To achieve this an application must be made to a Court having power to administer the Bankruptcy Acts to make the necessary orders. In the provincial districts of England this power usually rests with the County Courts, and in the Metropolitan District the High Court carries out the work.

**THE RECEIVING ORDER.**—A creditor may petition the Court to make a receiving order against a debtor, but before he can do so with success, he must satisfy the Court that he has a claim of not less than £50 which he is entitled to collect, and that his debtor has committed what is called an *act of bankruptcy*; that is to say, an act on which a petition may be founded.

The more usual acts of bankruptcy are—

- (1) The announcement by a debtor, to his creditor, that he is unable to pay his debts in full.
- (2) An assignment of his property to a trustee for the benefit of creditors; or if he makes any fraudulent gift or transfer of his property or any part of it; or if he fraudulently prefers one creditor to his others.
- (3) If, with the intent to defeat or delay his creditors, the debtor leaves, or remains out of England, or adopts any plan to avoid his creditors as when he absents himself from his dwelling-house, or shuts himself up in his dwelling-house and refuses to see creditors.

If the Court is satisfied that an act of bankruptcy has been committed, and that the petitioner is a creditor of £50 or more, a *Receiving Order* will be made, unless the petition is defeated when heard. Generally speaking, the Courts resent being used as a debt-collecting machine, and, therefore, it is a bad policy to receive anything on



account of a debt when once bankruptcy proceedings have been started. Not only will it invalidate the claim by altering the amount owing, but the probability is that, if it can be shown that the creditor petitioning for a receiving order is really seeking his own advantage and not the interests of the creditors in general, the receiving order will not be granted. The object of bankruptcy is to provide a means by which the available property of the debtor may be divided properly among all those who claim to be creditors.

**Effect of Receiving Order.** The effect of the receiving order, when granted, is to place an official known as an *Official Receiver* in possession of all the property of which the debtor is possessed, except property of which he is only the trustee. The debtor must also be allowed the tools of his trade, and the necessary wearing apparel and bedding of himself and his family, to an amount not exceeding £20. This illustrates the principle that it is against the interests of the community to deprive a person of all means of making a livelihood.

Of course, a debtor may himself petition the Court for a receiving order when he is in difficulties, and, in this case, the order will usually be granted. The effect is to put the Official Receiver in possession of the debtor's property. The Official Receiver is an officer of the State, and acts under the general control of the Board of Trade, by which he is appointed, but he is also subject to the directions of the Court. It is the Official Receiver's duty to take possession of the estate of any person against whom a receiving order has been made, and from that moment onwards—

(1) No one can effectively deal with the property except the Official Receiver.

(2) No one, other than the Official Receiver, can give a valid receipt on behalf of the debtor—not even the debtor himself.

(3) No one can get a valid title on buying a bankrupt's property except from the Official Receiver.

(4) Anyone trying to interfere with the Official Receiver in the execution of his duties can be charged with contempt of Court.

The Official Receiver collects the debts and realises the assets, and, after discharging the expenses and fees, distributes any balance amongst the creditors who have proved their debts.

**Proving a Debt.** A creditor must take steps to prove his debt as soon as possible after the granting of the receiving order. He must



submit an affidavit showing the amount of, and consideration for, his claim, and must submit any necessary documents in evidence, e.g. promissory notes. When the creditor is a limited company the proof must be made by some authorised agent on behalf of the company, for a company can act only through agents, e.g. the Secretary or Managing Director. The Official Receiver (or Trustee, if one is appointed to act instead of the Official Receiver by the creditors at their meeting) must give his decision on all proofs received, within twenty-eight days, but the decision is subject to revision by the Court, if necessary.

**LIQUIDATION.**—A company when once incorporated under the Companies Act, 1929, cannot be brought to an end except by removal from the Register of Companies on the ground of its being a defunct company, or through the machinery of winding up. The name of a company will be removed from the Register if no returns have been made and the Registrar is satisfied that the company is defunct.

A company may be wound up in one of three ways—

- (1) Voluntarily—without interference of the Court.
- (2) Compulsorily—by order of the Court.
- (3) Voluntarily—subject to the supervision of the Court.

**Voluntary Liquidation.** This is by far the most common method of winding up; about 90 per cent of companies that come to an end are wound up in this way. It is commenced, in every case, by the company passing an ordinary resolution, if the time for the company's duration has expired; or an event provided for by the Articles has occurred; or, an extraordinary resolution if the company cannot carry on business because of its liabilities; or, in any other case a special resolution.

If the directors are of the opinion that a company can pay its debts in full within twelve months from the commencement of the liquidation, a majority of the directors, or the two directors if there are no more, may declare and file with the Registrar of Companies a declaration to this effect. The liquidation will then be conducted as a "members' voluntary winding-up," but if no declaration is filed, then as a "creditors' voluntary winding-up."

*Members' Voluntary Winding-up.* A liquidator is appointed by the company at the meeting which is called for the passing of the resolution to wind up and at which his remuneration may be fixed.



The creditors have no right to interfere until twelve months have passed, the conduct of the liquidation being in the hands of the members. This form of liquidation has been specially designed for the purposes of amalgamation and reconstruction.

*Creditors' Voluntary Winding-up.* The company must summon meetings of its members and creditors, the creditors' meeting to follow the members' meeting not later than the next succeeding day, by notices sent out simultaneously and the creditors' meeting must be advertised in *The Gazette*.

The resolution placing the company in liquidation is passed at the members' meeting.

A director must preside over the creditors' meeting, at which a statement of affairs and list of creditors must be produced. The creditors have the power to nominate the liquidator and conduct the liquidation, usually by means of a *Committee of Inspection*.

The liquidator disposes of the assets in the most advantageous way and distributes the proceeds, after payment of all the costs of the liquidation, in discharge of creditors' claims and the surplus, if any, to the members.

**Compulsory Liquidation.** This is commenced by a petition to the Court presented either by a creditor, a contributory, or the company itself. On hearing the petition the Court usually make a winding-up order and the Official Receiver is generally appointed Liquidator. The Official Receiver obtains a statement of the company's affairs and renders a report to the Court, and, if necessary, he may request the public examination of any person connected with the company; the Court having power to grant his request. The Official Receiver must acquaint all creditors with the financial position and attend to the winding-up of the company, unless a liquidator has been appointed to do this. When the affairs of the company have been wound up the Court may make an order that it be dissolved, and it is dissolved accordingly.

**Liquidation Under Supervision.** The Court may make an order that a voluntary winding-up shall continue but subject to the supervision of the Court. Such an order has the advantage of operating as a stay of any actions or executions pending against the company. Except in these respects, the winding-up remains a voluntary one. The Court does not actively intervene unless set in motion.

**RECONSTRUCTION.**—A large number of companies now wind up



## COMPARISON OF DIFFERENT FORMS OF LIQUIDATION

Form	Circumstances Under which Applied	Conditions Rendering it Desirable	Effects
Voluntary Liquidation.	<ol style="list-style-type: none"> <li>(1) When the period fixed for the company's duration expires.</li> <li>(2) When the event which terminates the company's business occurs.</li> <li>(3) When by reason of the liabilities it cannot continue.</li> <li>(4) When the company for any reason requires a voluntary winding up.</li> </ol>	When it is desired to dissolve a company amicably, whether solvent or insolvent.	<ol style="list-style-type: none"> <li>(1) The company ceases to carry on business except for winding up purposes.</li> <li>(2) It remains a corporate body.</li> <li>(3) On appointment of the liquidator the director's powers cease.</li> <li>(4) Transfers are subject to the liquidator's consent.</li> <li>(5) If winding up lasts more than a year the liquidator calls meetings of the company at the end of each year.</li> <li>(6) The liquidator may settle the list of contributors, make calls and carry on the business for winding up purposes.</li> </ol>
Compulsory Liquidation by the Court.	<ol style="list-style-type: none"> <li>(1) When a special resolution of the company requires it.</li> <li>(2) When the company fails to commence business within one year.</li> <li>(3) When the company suspends its business for a year.</li> <li>(4) When the company is unable to pay its debts.</li> <li>(5) When the membership of the company falls below the legal limit.</li> <li>(6) When the company fails to file the statutory report or hold the statutory meeting.</li> <li>(7) When the Court is of opinion that it is just and equitable.</li> </ol>	When the company becomes insolvent.	<ol style="list-style-type: none"> <li>(1) The winding up order operates as a notice of discharge to all servants of the company because it affects the personality of the employer, the business being carried on by the Court.</li> <li>(2) All dispositions of the property of the company made between the commencement of the winding up and the winding up order are avoided.</li> <li>(3) A stay is put on all actions and executions.</li> <li>(4) The Official Receiver becomes the official liquidator, until another person is appointed.</li> </ol>
Liquidation under supervision of the Court.	On application the Court can direct that the voluntary winding up proceed under its supervision.	When it is desirable to put a stay on all proceedings against the company or to appoint a representative of the Court to act with the existing liquidator.	The liquidator appointed in the voluntary winding up may exercise all his powers without the sanction of the Court, but subject to such restrictions as the Court may direct.
Reconstruction.	When a compromise between a company and its creditors, or a reorganisation of the company is desired.	When it is desired to raise fresh capital by issuing partly paid up shares in the new company in exchange for fully paid up shares in the old company, or where it is desired to rearrange the capital of the old company.	<p>No member can be bound to take shares but each dissentient is protected and entitled to value (s. 105). A scheme excluding the rights of dissentients is <i>ultra vires</i>.</p> <p>Compromises are binding if agreed to by three-fourths of the members or creditors, subject to Court's sanction.</p>



only to reconstruct. The reason for reconstruction is usually to raise fresh capital. Reconstructions are carried out in one of three ways—

(1) By sale and transfer of the company's undertaking and assets to a new company, under Section 154 of the Act; or

(2) By sale and transfer under a power to sell contained in the company's Memorandum of Association; or

(3) By a scheme of arrangement, sanctioned by the Court under Sect. 153.

These different forms of winding up are compared in the table on page 867.

### TEST PAPER LXXIII

1. Does an insolvent person automatically become bankrupt?
2. State the ground on which a person can be made bankrupt.
3. What is meant by an act of bankruptcy? Mention any acts of bankruptcy.
4. Explain the effects of a receiving order.
5. What are the duties of an Official Receiver?
6. How does a creditor in bankruptcy "prove" his debt?
7. What are the chief duties of an Official Receiver?
8. You are a creditor of X and desire to present a bankruptcy petition against him. In what Court would you present it, and what are the essential requisites for the petition to be valid?
9. Explain three methods by which the existence of a company may be terminated in the process generally termed "winding up," pointing out the stages in which such methods are applied.
10. What is the difference between a members' voluntary and a creditors' voluntary winding-up?

### FINAL NOTE

Since many of the matters dealt with in a book of this character are subject to continual change, no textbook can hope to remain completely up to date for any period of time. The student should therefore cultivate the habit of watching the press for current developments, and compile a notebook to supplement his reading.



# COMMERCIAL AND ECONOMIC TERMS

**Adjudication Order.**—The order by which a person is adjudged a bankrupt and his property vested in a trustee, to be administered for the benefit of his creditors.

**Agio.**—The difference between the real and nominal value of money. When paper currency is depreciated, the agio represents the premium at which gold stands as compared with the paper.

**Alloys.**—The bodies resulting from the union of two or more metals, the union being brought about under the influence of a high temperature. The special properties of alloys depend quite as much upon the proportions in which they are mixed as upon the component metals themselves.

**Alpaca.**—The long, silky, lustrous wool obtained from the alpaca, an animal largely bred in Peru and other South American States. More than 2,000,000 lb. of this wool are imported annually into Great Britain.

**Angora.**—The name given to a breed of goats inhabiting Asia Minor. The finest type of wool is obtained from these animals, mohair being the principal. The chief seats of manufacture in England are Norwich and Bradford. A species of Angora goat has been bred in the United States, Cape Colony, and Victoria (Australia) for the sake of the wool.

**Aniline Colours.**—Owing to their great brilliancy, their diversity of colour and shade, and the ease with which they can be fixed, these colours have practically superseded all other dyes.

**Anthracite.**—The very best type of coal, much used for steam fuel. It is almost smokeless and contains 90 per cent. of carbon. It is largely worked in South Wales; the largest deposits are in Pennsylvania.

**Arbitrage.**—The operation of buying securities or produce in one market and telegraphing orders to agents to sell them in another market, whereby a profit is made on a difference in price due to the constant fluctuations in prices on the various Stock and Produce Exchanges of the world.

**Arbitrator.**—The person called in to give the decision when a dispute is settled by agreement or arbitration.

**Assignment.**—A transfer of title or of interest in any property.

**Average.**—The apportionment of expenses and loss occasioned in preventing total loss to a ship or cargo, over the various contributors. Where a sacrifice is made, such as the jettisoning of cargo to lighten the ship in a storm, for the benefit of all persons interested in the voyage, the loss is borne by all such persons in proportion to their interest in the venture.

**Average Bond.**—The document signed by contributors to a general average adjustment, under which they receive delivery of cargo on undertaking to pay their share of the general average contribution as soon as the amount is ascertained.

**Backwardation.**—The consideration paid by a "bear" operator on the Stock Exchange, when he desires to carry over (*i.e.* to defer delivery of shares).

**Bank of Issue.**—A bank which issues its own notes payable to bearer on demand.

**Barley.**—The product of one of the cereal plants. Large quantities are raised in the United Kingdom, and considerable imports are received from Denmark, Siberia, United States, Canada, and Mexico. Principally used in Great Britain for malting purposes.



**Beet.**—The plant from which beet-root is obtained. The Silesian beet is the most valuable, as being the most productive of sugar. It has been estimated that one-half of the sugar of the world is made from the Silesian beet.

**Bessemer Steel.**—Steel made direct from cast iron by a process patented by Sir Henry Bessemer in 1856. The pig iron in a molten state is placed in a converter and subjected to a blast of air at high pressure. Bessemer steel is employed in the manufacture of heavy articles, especially rails, rollers, boiler plates, ship plates, etc.

**Bonded Warehouse.**—A secure place sanctioned by the Board of Customs for the deposit of dutiable goods without payment of duty until they are removed.

**Bottomry Bond.**—The undertaking given by the captain of a ship which requires immediate repairs, and the necessary money for which is the consideration for the Bond. The payment under the Bond is enforceable only if the ship reaches port safely and when the consideration has consequently been of benefit.

**Bourse.**—The name given to a Continental Stock Exchange or Money Market.

**Brick Tea.**—The name given to tea which is compressed into blocks or slabs. There is a large trade in this tea between China and Russia, but the article does not enter British commerce.

**Bristles.**—The stiff hairs of various animals, especially those of the wild boar and the hog. Imported into England for brush-making, and also used by shoemakers and saddlers. Imported chiefly from Russia.

**Bullion.**—Gold or silver in bars or in the mass, as distinct from the coined metal.

**Cambist.**—A term applied to one who exchanges foreign money or deals in foreign notes or Bills of Exchange.

**Caoutchouc.**—An important elastic gum, commonly known as india-rubber. It is the sap which is obtained by the tapping of a species of tree grown in the tropics. After the drying process, the sap or juice thickens, and when carefully prepared is white in colour, but it is usually brown or brownish-black. It is lighter than water. The principal supplies come from Brazil.

**Cheap Jack.**—A kind of travelling hawk who hires a shop in a good position and obtains his stock chiefly from auction sales and bankruptcy stocks. By employing various forms of propaganda he sells his stock as quickly as possible and, when business ceases to pay, moves to another district.

**Cheap Money.**—Cheap money conditions prevail when loans are easily obtained and the interest correspondingly low.

**Cheque Rate.**—A term used in connection with the Foreign Exchanges. It indicates the price at which a cheque or sight draft upon another country may be purchased.

**Circular Notes.**—These are modified forms of letters of credit issued by banks in return for money deposited with them. With the circular notes cheques are supplied, which can be drawn on the grantor up to a stated sum. Each draft, when cashed, must be endorsed by the paying banker and the signatures of the holder compared with those in the letter of credit. Sometimes notes for stated amounts are issued addressed to a bank's foreign agents, together with a letter of indication to assist identification. This form is particularly suitable for travellers abroad.

**Coal.**—The chief fuel substance. It occurs in beds varying in thickness from a few inches to several feet. The deposits were originally the remains of vast forests, the chemical composition of which has undergone a complete change. Principal varieties—

1. Brown or impure substance.
2. Bituminous, containing 88 per cent. of carbon.
3. Anthracite, the best kind, containing 90 per cent. of carbon.



4. Cannel, compact and lustrous, burns with a bright flame ; mostly used in the manufacture of gas.

**Cocoa.**—A commodity used in the preparation of a beverage. It is the seed of a tropical tree cultivated in the West Indies, tropical America, Asia, and Africa. Within the seeds are the cocoa nibs of commerce. The chief supplies are obtained from Trinidad and the States of Central America.

**Coffee.**—The berries of the coffee plant, cultivated in Abyssinia, tropical Asia, and America. The value of the coffee consumed annually is £60,000,000. India, Ceylon, Java, Brazil, and Arabia are the chief exporting countries.

**Coke.**—The residue left when coal has been deprived of the greater part of its hydrogen, oxygen, and nitrogen. Chiefly obtained as a by-product in the manufacture of gas for illuminating purposes.

**Collectivism.**—A form of socialism which would have all the means of production and distribution, land, machinery, and capital in the hands of the State, and operated by the general will for the common good.

**Contango.**—The consideration paid by a "Bull" operator on the Stock Exchange when he "carries over," and consequently postpones payment of his purchases. It is interest on the money required to keep control of the stock which is the subject of the "Bull" speculation.

**Copper.**—The earliest metal known : valuable in the manufacture of bronze. Principal ores widely distributed ; great deposits in United States. Largely worked in Swansea and neighbourhood, their supplies being drawn from Cornwall, Spain, Portugal, and Australia. The alloys of copper are of enormous importance in manufactures. The chief are bell-metal, brass, bronze, and gun-metal.

**Cost Accounts.**—These are records specially compiled for the purpose of showing, in a convenient form, the various items of the cost of working any undertaking engaged in the production of commodities or in the performance of any work involving the employment of manual labour and the use of materials.

**Cotton.**—One of the most important of vegetable fibres ; cultivated extensively in tropical countries. The seeds are picked and the fibre removed by the process of "ginning." The cotton is afterwards compressed by a screw or hydraulic press into bales of from 300 lb. to 600 lb. each. There are many kinds of cotton, American sea-island cotton being the finest. Considerable attention paid to cotton growing in Egypt and in our Colonies. Principal supplies from the United States. The county of Lancashire is the great producing centre of cotton goods.

**Countervailing Duty.**—A customs tax imposed on imports so as to place them on an equality with the home products that are liable to excise tax.

**Currency.**—The means whereby commodities are exchanged by purchase and sale, without recourse to barter. The commodities are measured by currency units, and the amount fixed on each commodity is called the price. Currency is thus the medium which circulates in a country for the purpose of settling indebtedness. Gold is the standard currency of most civilised countries and is the basis of their payments, though the majority of commercial transactions are settled by means of "representative" currency, such as cheques and Bills of Exchange.

**Custom House.**—The place appointed by the Government for the purpose of imposing and collecting the duties placed upon certain imports.

**Cutlery.**—The general name given to cutting instruments, such as knives, forks, scissors, razors, etc. Sheffield is the centre of production for England. France, United States, and Germany are keen competitors.

**Dead Freight.**—When a charterer has failed to provide a full cargo for the vessel chartered, the loss thus accruing to the shipowner must be made up by the charterer, and this is called "dead freight."

**Debit Note.**—A document sent by a trader to a person from whom he has



bought goods which are unsatisfactory, stating the amount of the deduction he wishes to be made from the account.

**Decreasing Returns, Law of.**—This is perhaps the most far-reaching law in economics, and operates chiefly in the extractive industries. It states that after a certain stage of development every increase in the output will be obtained at a more than proportional increase of cost, unless the means of production have meantime been improved.

**Deficiency Bills.**—The bills created when the Government Funds in the hands of the Bank of England are insufficient to pay the quarterly dividends, the balance being borrowed from the Bank of England. They are drawn for less than three months, and the rate is half of the prevailing discount rate of the Bank of England, with a maximum of 3 per cent.

**Drawback.**—The return of duty on the export of excisable commodities and on the re-export of commodities on which Customs duties have been paid.

**Economy.**—"The administration of any kind of resources (time, thought, or money, for instance) in such a way as to secure their maximum efficiency for the purpose contemplated. It is administration with a minimum of waste." (Wicksteed.)

**Embargo.**—The Government Order under which ships are detained in port or excluded from a port. Frequently resorted to in time of war, or to prevent undesirable cargoes from being imported from abroad, as in the case of diseased animals.

**Enticed Paper.**—A term given to the promissory notes of the Indian Government (known in the market as "Rupee Paper") when they bear a notification that the interest upon them can be collected by presenting the notes at the Bank of England.

**Entrepot.**—A warehouse used in transshipment trade. The goods remain in the warehouse until their journey is resumed.

**Esparto.**—A species of grasses found in various countries bordering the Mediterranean, long been used for the manufacture of carpets, baskets, ropes, nets, etc. Chiefly used now in paper-making. Great Britain largely imports from Algiers.

**Exchange.**—This branch of economics embraces the sum total of all the relations and institutions which link together the various economic units. The organisation through which this exchange takes place is *the market* which may be defined as that area whether large or small, within which every portion of the supply of a commodity is equally available to each portion of the demand.

**Expansive Theory.**—The theory that the Bank of England should expand its issue of bank notes, in times of crises. The restrictions of the Bank of England in the issue of notes have been removed occasionally in times of monetary crises, and in more than one case the mere knowledge of such removal was sufficient to restore confidence. Hence, the expansive theory has been justified. Recourse to the method was not necessary at the outbreak of the Great War, Treasury Notes being issued instead.

**Fiduciary Issue.**—The name given to the Bank of England Notes issued against first-class securities instead of gold.

**First-class Paper.**—Treasury Bills and bills which bear the names of banks and financial houses of the very highest standing.

**Flax.**—The fibre obtained from the common flax plant grown largely in Russia, Saxony, Belgium, Holland, Italy, and North of France; still considerable crops raised in Ireland. Used in the manufacture of linen. The seeds of the plant are used for the manufacture of linseed oil.

**Funded Debt.**—The permanent loan of the British Government. No fixed date of redemption is stated, the bonds being redeemed as the revenues of the country permit. A Sinking Fund has been created for this purpose.

**Fur.**—The short, fine, soft hair of certain animals, growing thick upon the



skin ; provides the warmest kind of clothing. The furs of the larger kind chiefly obtained from Siberia and North America ; smaller varieties from various parts of Europe.

**Glucose.**—The ordinary glucose occurs in the juices of ripe fruits, generally obtained as a saccharine product from maize, potatoes, or other starchy substance by the action of sulphuric acid. Imported from Germany, France, and United States ; used by brewers.

**Godown.**—A warehouse in the East where imported goods are stored until required for use.

**Gold.**—The precious metal employed for coinage, ornaments, plate, and jewellery. For the last half-century, Australia, California, and, lately, South Africa, have supplied the demands of the world. It is found in the form of either grains or nuggets. Gold can be beaten into leaves so fine that light can be transmitted through them. Pure gold is said to be of the fineness of 24 carats. It is too soft to be used in its pure state. An alloy of 22 parts gold and 2 parts copper is used for gold coinage. In jewellery, there are various standards, the most usual being 18, 15, and 9 carats.

**Gold Bonds.**—Bonds issued by the various American Railway Companies, which are payable in gold coin, either in New York or at a fixed rate of exchange in London.

**Greasy Wool.**—The wool or fleece of sheep when shorn and still unscoured. The majority of the Australian and Cape wool comes in a greasy condition. Considerable judgment has to be exercised by wool buyers, as the quantity of dirt in a particular consignment varies considerably, and an error of even 1 per cent. in estimating the yield of wool would result in a bad bargain.

**Gresham's Law.** This was first propounded by Sir Thomas Gresham, a London merchant, who assisted Queen Elizabeth with the re-coinage of silver in 1560. The law states that where two coins of the same metal are in circulation, one better than the other, the full weight coin will be held back by bankers, bullion dealers, and others, while the poor coin will be passed on and used as currency. In other words, the bad money will drive out the good. Secondly, in a bi-metallic currency, wherein the market value of the two metals, for example, gold and silver, fluctuates daily from the ratio as fixed by law, the over-valued metal, that is, the cheaper form of currency, will drive the under-valued metal, that is, the dearer form of currency, out of circulation.

**Gunny Bags.**—Sacks woven from the coarse fibre of the jute plant. The bags and sacking are largely exported from India to the United States, Australia, and Straits Settlements. The trade has developed considerably in recent years : the bags are mainly used for wool-packs, sacks for grain, seed, and salt.

**Hair.**—Apart from the hair of animals used in certain manufactures human hair is a commodity of no little importance. Great Britain's imports come chiefly from France, Germany, India, and China. Used in making wigs.

**Hammered.**—A member of the Stock Exchange is said to be hammered when he is expelled from membership of the institution through inability to fulfil his obligations, being unable either to pay for securities bought or to deliver shares sold.

**Hardware.**—The general trade name for all kinds of articles manufactured from iron, steel, brass, copper, etc. ; especially ironmongery, cutlery, and implements. Chief English centres of manufacture : Birmingham, Sheffield, Wolverhampton.

**Hawker.**—According to the Hawkers Act, 1888, this is "anyone who travels with a horse or other beast of burden selling his goods." As a rule, hawking tends to be restricted nowadays to the sale of agricultural produce such as greengrocery, and the sale of baskets and chinaware.



**Herring.**—The well-known fish caught in great shoals for food. Herring fisheries chiefly conducted off the coasts of Great Britain, Norway, and Newfoundland. Home consumption cannot be estimated; export trade increasing, chiefly to Germany and Russia. Grimsby and Yarmouth are the chief centres in England; Stornoway, Wick, Fraserburgh, Peterhead, and Aberdeen the chief Scotch centres.

**Hire-purchase Agreement.**—A contract by which a customer takes immediate possession of certain goods in return for an agreement to pay for them by periodical instalments, the goods remaining the property of the seller until all the instalments have been paid. Thus it is a system by which future income is mortgaged to pay for articles which are required for immediate use. Hire purchase agreements were at first employed to facilitate the purchase by manufacturers of expensive plant and machinery, but has gradually been extended to the purchase by the general public of such articles as furniture, motor cars, wireless, and other durable commodities.

**Hosiery.**—The name applied to undergarments generally, made of cotton, wool, or silk. Nottingham and Leicester, in England, and Hawick, Scotland, are the centres of manufacture. Export trade considerable.

**Inconvertible Paper Currency.**—Paper money which cannot be accepted as representing its face value.

**Increasing Returns, Law of.**—One of the most important laws in economics. It is sometimes known as the law of the factory, and arises when the market is large, being limited by the extent of the market and the nature of the occupation. It so operates that every increase in the supply of a manufactured commodity tends to be produced at a less than proportionate increase of cost.

**Indigo.**—The important dark-blue dye-stuff obtained from certain tropical plants. Best indigo prepared in Bengal. Indigo is the best substance for dyeing woollen cloth and for calico printing. Latterly, artificial indigo has been obtained from a coal-tar product.

**Iron.**—The most important of the minerals of the earth; distributed all over the world; in some parts in enormous deposits. The iron of commerce is obtained from the deposits of iron ore; total yearly production approaches 200 million tons, of which United States produces two-fifths, Germany one-fifth, and Great Britain one-eighth.

Iron is obtained from its ores by smelting with coal or coke in blast furnaces. The various kinds of iron are: cast iron, steel, and wrought iron, depending upon the amount of carbon contained in it. The uses to which iron is put are too well known and too numerous to be stated here.

**Ivory.**—The general name for the white dentine on the teeth and tusks of certain large animals, such as the elephant, walrus, and hippopotamus. The ivory of commerce chiefly obtained from the tusks of elephants; shipped mainly from Zanzibar and Pemba: about 40,000 elephants killed annually in Central Africa to supply European markets.

Ivory is a favourite substance for making ornaments; in great demand for pianoforte keys, billiard balls, carved figures. Principal seat of the carved ivory trade is Dieppe. Half of the world's ivory product is taken by English manufacturers.

**Jerquer.**—A Customs official whose duty it is to examine the ship's cargo, to prevent goods being imported without paying duty.

**Jewellery.**—Articles manufactured in precious metals, precious stones, and other valuable materials, used for purposes of adornment. Amsterdam is the centre of the diamond-cutting trade. Birmingham is the city where most of the cheaper jewellery is made. In the better classes of jewellery, the manufacturers of Clerkenwell, in London, have the highest repute in the United Kingdom.



**Kaolin.**—A very pure white clay, commonly known as china clay. On account of its purity, it is valuable in the manufacture of china and the finest kinds of porcelain. Since 1755, at which date deposits were found in Cornwall, the chief British supplies have been obtained from that county.

**Kite-flying.**—Dealing in fictitious or accommodation bills in order to raise money to keep up one's credit.

**Lead.**—A metal used very extensively for piping and the manufacture of bullets. Remarkable for its softness. It is not a good conductor of either heat or electricity. In Great Britain the chief supplies are from the Cumberland mines. Lead enters into the composition of several useful alloys, the most important being type metal, stereo metal, plumber's solder, pewter, and shot metal.

**Leather.**—The hides or skins of animals which have been subject to certain chemical processes by the operation known as tanning, whereby they are given increased strength, toughness, pliancy, and insolubility in water. Apart from the various market hides (i.e., those received from the various slaughter-houses of the country), the main imports are received from South America. As a preliminary to being tanned, the hides are salted, so as to preserve them from putrefaction. Leather is put to many uses: boots, shoes, gloves, saddlery, etc.

**Linen.**—The fabric manufactured from the fibres of flax and hemp. A most important industry of the United Kingdom; centres of manufacture: Belfast, Leeds, and Dundee. Many other large towns also engaged in linen manufacture. The various linen textures include fine lawns and cambrics, damasks, diapers, shirtings; and, among heavier fabrics, sail-cloths and canvas.

**Ling.**—A variety of cod fish taken in large quantities off the British coast.

**Localisation of Industry.**—This is the tendency of industries to be carried on and developed in those districts which are most suited to them and most likely to make them profitable. The following are some of the chief factors which account for such localisation—

1. Proximity to raw materials.
2. The presence of suitable sources of power.
3. A suitable climate.
4. Good means of communication.
5. Adequate supplies of labour and capital.
6. To make machinery for an industry already established.
7. Proximity to markets.
8. Force of custom.

**Maize.**—A well-known cereal, commonly known as Indian corn: one of the most important grain crops in the world; grown chiefly in the United States. In Britain it only thrives in favourable summers.

**Making-up Price.**—The price fixed by the Committee of the Stock Exchange for the carrying over of bargains. It is also the price at which the differences of stocks are transferred through the Clearing House.

**Manifest.**—A declaration made to the Customs House officials concerning a cargo of a vessel.

**Marginal Letters.** These are letters of credit which have blank forms of bills attached to the margin of the letter. The foreign agents sign and otherwise complete them when advances are made.

**Merino.**—The name of a choice breed of Spanish sheep celebrated for their long, fine wool. The merino has been introduced into Australia and South America, from which places the chief supplies are now obtained.

**Metrie System.**—The name given to a system of weights and measures in use in France, Belgium, Holland, Spain, Italy, Portugal, Greece, and other countries, the metre being taken as the unit. There are four principal



units, with their decimal multiples and fractions, in the system, viz.: the *metre* for length, the *are* for surface, the *litre* for capacity, and the *gramme* for weight. The fractions are denominated by syllables derived from the Latin, *deci*, *centi*, and *milli*; the multiples by the syllables (borrowed from the Greek) *deca*, *hecta*, *kilo*, *myria*, representing tens, hundreds, thousands, and tens of thousands, respectively. The great advantage rests in the rapidity of calculation which is possible when transferring quantities from one denomination to another, owing to the fact that each lower unit is exactly one-tenth of the one immediately higher. All that is necessary is to remove the *decimal point* one or more places to the right or left, according to the denomination required. The equivalents in English measures of the various units in the metric system are approximately as follow—

An inch	is about	25 millimetres
a foot	„	30 $\frac{1}{2}$ centimetres
a yard	„	·914 metres
a quart	„	1·136 litres
a pound (avoir.)	„	·454 kilogram
an acre	„	·405 hectare

**Monometallism.**—The system under which the standard coins of the country are of one metal only, other coins being token money and not standard money.

**Moratorium.**—An extension of time allowed under exceptional circumstances by the Government of a country for the payment of debts.

**Mungo.**—The waste produced in a woollen mill from hand spun or felted cloth, or from the tearing up of old cloths: used for the manufacture of shoddy. (See SHODDY.)

**Muslin.**—A fine cotton fabric. Some of the finest muslins are made in India, but Manchester and the surrounding districts supply various kinds of muslin for all parts of the world.

**Myrrh.**—The gum-resin obtained from a tree growing in Arabia and Abyssinia. It is composed of resin, gum, and an essential oil, with a small quantity of mineral matter. From the earliest times myrrh has been used for burning as incense. Medicinally, it is now employed as a stimulating tonic, and as an ingredient in the manufacture of dentifrices.

**National Debt.**—The entire debt of the nation, that is, money borrowed at various times by the Government for national purposes.

**Oats.**—A well-known cereal, widely distributed over the temperate and cold regions of the globe. In the United Kingdom, the supplies of home-grown oats are double those of wheat. Considerable imports from Northern Europe, particularly Russia. The grain is principally used as a horse food, but is a valuable human food-stuff when ground into meal.

**Oils.**—The name applied generally to all viscous fluids (i.e. those which do not flow readily). They are divided into two main groups, fixed oils and essential oils. Essential oils are generally obtained by distilling the leaves, flowers, etc., of plants with water, and they may be distilled without undergoing much change. Most essential oils have a powerful odour, which varies according to the nature of the plants from which they are obtained.

Fixed oils cannot be distilled without undergoing decomposition. They are divided into the two classes of vegetable and animal oils, according to their origin. A further division of fixed oils is into those of drying and non-drying oils. Drying oils are mainly used for mixing painters' colours. The non-drying oils are employed for illuminating purposes and soap-making, the chief of these oils being olive, almond, ben, laurel, rape, palm, and candle-nut.

**Omnium.**—The aggregate value of the different kinds of stock which form a loan.



**One Man Company.**—The name given to a limited company the shares of which are practically all held by one man. Six other shareholders are allotted an insignificant number of shares to make up the necessary seven shareholders required for a public company by the Companies Act.

**Pari Passu.**—In equal proportions.

**Parity.**—The prices of American securities as quoted on the London Stock Exchange, the dollar being taken at 4s. for ease in calculation. Thus, a security quoted at 4 dollars in America will be quoted at about 4½ dollars in London.

**Pedlar.**—According to the Pedlars Act, 1871, a pedlar is "any hawker, pedlar, petty chapman, tinker, caster of metals, mender of chairs, or other person who, without any horse or other beast bearing or drawing burden, travels and trades on foot and goes from town to town or to other men's houses, carrying to sell or exposing for sale any goods, wares, or merchandise . . . or selling or offering for sale his skill in handicraft."

**Petroleum.**—Also called rock oil. It is a thick oil, and is found chiefly in the United States, Canada, and Russia. In its original state it is unfit for use and requires to be distilled, from which process three products are derived. The first consist of light oils, such as benzoline, which are highly inflammable and dangerous as illuminants. The second, or refined petroleum, are the illuminating oils. The third are the heavy oils used for lubricating purposes. The by-products are very numerous and include dyes, carbolic acid, aniline saccharine, vaseline, etc.

**Pottery.**—This is the name given to all vessels made from earthy materials, especially clay, for use or for ornaments. A rough division is made between hard and soft ware, the former including hard porcelain, European porcelain, biscuit porcelain, and stoneware; and the latter, majolica, common earthenware, and terra-cotta.

**Power of Attorney.**—The document by which a person is specially empowered to act for another in the capacity or capacities stated in the attorney.

**Profit Sharing.**—The system under which labour receives, in addition to ordinary wages, a share of the profit which the business realises.

**Protection.**—A tariff policy for the encouragement of home industries either by—

1. Absolute prohibition of the import of competing foreign articles.
2. The manipulation of the tax system to place restrictions on the import of foreign commodities.
3. The payment of bounties on the productions of the home country.

**Pyx.**—The box in which are preserved samples of coins made at the Mint. A jury of the Goldsmiths' Company, who are summoned by the Lord Chancellor, test the coins annually at what is called the "Trial of the Pyx," to see that the legal weight and fineness of the coins are maintained.

**Racking.**—The term applied at the Custom House to drawing off, transferring, or combining wines or spirits from casks.

**Rack Rent.**—An annual rent extended to the full value of the thing rented. The highest rent which the land will bear.

**Rags.**—The remains of discarded woollen and cotton clothing. Linen and cotton rags are still used for the manufacture of the best kinds of paper; woollen rags for shoddy. Great Britain imports largely from the Continent, and re-exports about one-half of the whole she receives to the United States.

**Rationalisation.**—The methods of technique and organisation designed to ensure the minimum waste in industry of either effort or material. It includes the scientific organisation of labour, standardisation both of material and products, simplification of processes, and improvements in the system of transport and marketing.



From this definition it will be seen that rationalisation is a very wide term indeed, and may manifest itself in a variety of ways according to circumstances. In one sphere it may consist in the application of the principles of scientific management in the light of modern conditions in order to secure the maximum return by the harmonious co-operation of the factors of production. It may involve standardisation and simplification leading to the economies of mass production. Again it may refer to the amalgamation and consolidation of business undertakings in the same or allied industries into one great unit under a centralised control, in order to reap the benefits of large-scale production. Or, again, it may affect the selling organisation and take the form of an elaborate system for the regulation of price, or the flow of supplies to the market.

**Reciprocity.**—The term given to the arrangement between countries, under which each agrees to admit the goods of the other upon special terms as regards Customs duties.

**Rente.**—The term applied on the Continent to the National Debt, as, for example, "French Rentes," which are equivalent to our Consols.

**Reserve Liability.**—That portion of a company's subscribed capital which can be called up only on the winding up of the concern.

**Restrictive Theory.**—The theory embodied in the Bank Charter Act of restricting the issue of bank notes. (See the **EXPANSIVE THEORY** for the converse.)

**Reversion.**—This is the right to property on the occurrence of a certain event such as death, expiry of a lease.

**Rice.**—A grain closely resembling barley in appearance. One of the most important of human foods; grown extensively in all tropical and sub-tropical countries; also Spain, Italy, and Austria. In great demand for the manufacture of starch. The refuse of rice forms a valuable cattle food.

**Rig.**—The secret operations of "Bulls" whereby the price of a security is forced up artificially. It is the manipulation of the market by "Bull" speculators for their own profit.

**Ring.**—A combination formed for the purpose of withholding the supplies of a commodity with a view to forcing up the prices. The operations of the Ring are known as "Cornering" the market.

**Rummaging.**—The name given to the searching of a vessel by the officers of the Custom House for the purpose of ascertaining that neither dutiable nor prohibited goods are concealed on board.

**Rupee Paper.**—(See **ENFACED PAPER**.)

**Rye.**—An edible grain of the wheat and barley species. Grown extensively in most parts of the Continent, rye bread being a commoner food of the peasantry abroad than wheaten bread. In England, it is grown only for fodder for cattle.

**Seigniorage.**—The profit made by the Government on the manufacture of token money.

**Ship's Protest.**—The document signed by the captain of a vessel, containing a declaration under oath as to the true circumstances under which damage to ship or cargo has been sustained. A copy is usually required when a claim is being made under an insurance policy.

**Shoddy.**—A material produced in Lancashire and Yorkshire and largely used in the manufacture of cloth. It is made of the wool obtained from worn and ragged woollen goods, with the addition of a certain amount of fresh wool. Shoddy has not the durability of new wool.

**Silk.**—The fibre of the cocoon of the silk-worm. It is the strongest, most lustrous, and most valuable of all textile fabrics. Manufacture of silk and silk goods is carried on mainly abroad, the principal countries being France, Belgium, and Holland.

**Silver.**—The well-known beautiful hard white metal. The most productive



ores in the British Isles are found in the Isle of Man. In Europe, it is found in Spain, Austria, and Germany. The great deposits, however, are in the United States and Central America. Silver is the best known conductor of heat and electricity and, consequently, is much employed in the manufacture of delicate electrical instruments and machines. Many valuable ornaments and household utensils are manufactured from this metal, which is also utilised in the manufacture of coins.

**Simplification.**—This is the process of eliminating all varieties of a product which cannot be justified on substantial grounds such as economy of production, proportion of sales, and so on. The process is very similar to standardisation but a distinction may be drawn. Simplification reduces the number of varieties, designs and styles whilst standardisation establishes these standards of size and design. Thus, in the American paving brick industry simplified practice led to the reduction from 66 to 4 varieties, but standardisation in hardness, composition and durability has not yet been achieved.

**Sliding Scale.**—An arrangement under which the remuneration paid to workmen increases with the advance, and reduces with the reduction, in the selling price of the manufactured article.

**Slinging.**—A shipping term used in some ports of the United Kingdom, meaning a charge for putting the chains around the goods as they lie in craft alongside the ship, to facilitate the hoisting of the goods on board.

**Stag.**—A person who applies for an allotment of shares in a new issue in the hope of being able to sell at an increased price to a disappointed applicant.

**Standardisation.**—In general terms, this denotes the preparation and application of definite specifications which are either compulsorily enforced or voluntarily adopted in connection with production or manufacture. In practice, standardisation is the selection of a small number of types or sizes that are most suitable and the specifying of them in every possible instance, so as to secure uniformity of production on a large scale. The process of standardisation is attended by the following economies—

1. Productive capacity is increased since mass production becomes possible.
2. Elimination of waste of material.
3. Reduction of stocks of raw material.
4. Reduction in cost of testing and inspection.
5. Reduction of storage space for finished goods.

**Steel.**—One of the three varieties of iron, the others being wrought iron and cast iron. It is formed from wrought iron under the action of great heat in blast furnaces, when it becomes fine-grained instead of fibrous. When steel is quickly cooled, it becomes very hard and brittle and is specially adapted for making cutting tools. (See BESSEMER STEEL.)

**Straw.**—The dried stalks of various cereals. Used in agriculture as bedding material and the making of farmyard manure; valuable for packing, thatching, making door-mats, baskets, mattresses, etc. It is a paper-making material. Enormous quantities used in straw-plaiting in the hat manufacturing trades. Luton is the centre of this industry.

**Sugar.**—The familiar food commodity which occurs in the juices of many plants, but which is prepared for commerce almost exclusively from the sugar-cane and the beet-root. The manufacture of sugar from the beet-root has long been an important industry of France, Germany, Austria, and Russia.

**Supply and Demand, Law of.**—The value of a given commodity in a given market at a particular time depends upon the relation between the supply of, and the demand for, that commodity; and every factor which influences, directly or indirectly, either the supply of the commodity or the demand for it, will similarly influence its value.

**Tale Quale.**—When goods are sold "to arrive," this expression signifies



that the goods are equal to sample when shipped, but the buyer takes the risk of any damage or deterioration during transit.

**Talon.**—The slip attached to a bearer bond. It is used in applying for further interest coupons when the previous issue is all used.

**Tea.**—The dried leaves of the tea plant of China and India. One-half or the supplies of the world are now obtained from the Indian Empire. The leaves of the plant are picked by hand and subject to various processes, drying by exposure to air, roasting, rolling by hand, and again roasting over charcoal fires. Tea forms one of the commonest articles of consumption.

**Tied Shop.**—One which, although not necessarily under, is generally controlled in some degree by a proprietary interest. It differs from the multiple shop inasmuch as the shopkeeper is not the employee of the interest to which the shop is tied. While retaining control of his business, however, he is bound to stock certain specified goods, and to further their sale in preference to that of other goods.

**Tin.**—A very malleable, lustrous, white metal. Found in the form of tinstone in Cornwall, and Devonshire, the Malay Peninsula, and Australia. It is a component of various alloys, the most important being gun-metal, bell-metal, solder, pewter, and bronze.

**Tobacco.**—The dried leaves of the tobacco plant, which grows both sides of the Equator. To prepare it for market, the leaves of the tobacco plant are cut, dried, and stripped. The leaves are generally allowed to be in heaps for a week or two and covered over, during which period a slight fermentation takes place. The subsequent treatment produces varieties of tobacco: Cavendish, shag, twist, etc. Great Britain's chief supplies are from America.

**Unified Stock.**—A name given to the several loans, bearing different rates of interest, which have been amalgamated into one common debt, bearing a fixed rate of interest, in a similar manner to our Consols.

**Watering Stock.**—The creation of new capital not for a legitimate extension of the concern's operations but, it may be, to make up for a depreciation in the assets representing previous capital.

**Wheat.**—The most important food grain of commerce. It is more grown in temperate parts than any other grain. It is a valuable flesh-forming and nutritive substance. Grown largely in England, but equally large quantities imported from the United States, Russia, Roumania, and India. The crushed grain of the wheat is flour.

**Window-Dressing.**—A term sometimes used in the money article to indicate that the banks are calling in loans in order to make their cash balances appear large in the periodical statements issued by them.

**Wood Pulp.**—A valuable commercial article used for paper-making. The pulp is obtained from the pine tree. Exported chiefly by Norway and Sweden.

**Wool.**—The hairy covering of certain animals, used for the manufacture of various fabrics. Next to cotton, it is the most important of all fibres. Chief supplies come from the sheep, though the wool of the alpaca, the Angora goat, the camel, and the mohair goat is also used largely. The greater portion of sheep's wool comes from Australia and South Africa. London is the greatest wool market in the world.

**Yarn.**—The name given to any textile fabric prepared for weaving into cloth. It is produced entirely by spinning machinery; Great Britain supreme in its manufacture for export as well as home consumption.

**Zollverein.**—The union of the various German States to enable them in their commercial dealings to act as one.



# EXAMINATION PAPERS

## RECENT EXAMINATION QUESTIONS

SET BY THE

UNION OF LANCASHIRE AND CHESHIRE INSTITUTES,  
THE ROYAL SOCIETY OF ARTS, AND OTHER BODIES

1. What do you understand by "Production"? Show that Commerce is a branch of production. (L. & C.)
2. To what branches of production do the following occupations belong? Mining, stockbroking, the grocery trade, architecture, engine-driving, cotton, spinning, acting. (L. & C.)
3. What do you understand by the term "Capital"? Of what elements might the capital (a) of a retail business, (b) of a manufacturing firm, consist? (L. & C.)
4. Carefully distinguish between fixed and circulating capital. (L. & C.)
5. Write a full note on one only of the following—
  - (a) Limited partnership.
  - (b) Distinctive differences between a limited liability company and an ordinary partnership. (L. & C.)
6. What is a "Private Limited Company" as defined by the Companies Act? Describe briefly the advantages and privilege of companies of this type. (S. of A.)
7. Take any article of manufacture in your possession and trace out
  - (a) The sources of its raw materials.
  - (b) The principal centres of its manufacture.
  - (c) The chief markets for the finished article. (L. & C.)
8. What are the qualifications of a successful *entrepreneur*? (L. & C.)
9. What is a broker? What are his principal functions? (S. of A.)
10. What is a limited partnership? When is this form of combination preferable to (a) an ordinary partnership, (b) a limited company? (S. of A.)
11. What purposes does Capital serve in business? What is Capital? (S. of A.)
12. What is Goodwill, and how is it affected by (a) advertising, (b) management? (S. of A.)
13. How would you distinguish between "Industry" and "Commerce"? Give two examples of each. (S. of A.)
14. Under what headings would you classify each of the following as occupations?—

(a) Coal-mining	(c) Teaching	(e) Banking
(b) Fisheries	(d) Insurance	(f) Accountancy

(S. of A.)
15. How is business affected by invention (a) in manufacture? (b) in distribution? (c) in the organisation of methods? (S. of A.)
16. What are the functions of Capital in business? (S. of A.)
17. What purpose is served by attempting to classify occupations? How would you subdivide "Commerce"? (S. of A.)
18. What are the functions of the *entrepreneur*? (S. of A.)
19. What are the functions of a Commission Agent? (S. of A.)



20. How far may borrowed Capital be employed in business with safety ?  
(S. of A.)
21. How does an extractive industry differ from a constructive industry ?  
(S. of A.)
22. What part does Banking play in Commerce ?  
(S. of A.)
23. How is Insurance connected with Commerce ?  
(S. of A.)
24. To what extent is the advance of Commerce dependent on the extension of geographical knowledge ?  
(S. of A.)
25. Write an order for goods from a retailer to a wholesale warehouse, and an acknowledgment of the receipt of the order in such a way that a contract results. Be careful to word the order in specific terms. (L. & C.)
26. What is a Tender ? Draft an estimate for the supply of any goods, material, or work with which you are familiar. (L. & C.)
27. Write a short account of the historical development of the retailer from the mediaeval craftsman. (L. & C.)
28. What are profits ? Distinguish between gross and net profits, and state their relation to turnover and working expenses. (L. & C.)
29. What are the characteristics of a good salesman ? (L. & C.)
30. What are the advantages and disadvantages of the multiple shop system ? (L. & C.)
31. State some methods by which orders for foreign trade may be procured. (L. & C.)
32. Enumerate and explain the principal forms used in business in the execution of a purchase or sale on credit. (L. & C.)
33. Compare and contrast the following forms of business organisation—  
(a) Sole trader (b) Limited company (L. & C.)
34. What different methods—direct or indirect—are open to the producer in the distribution of his goods to the consumer ? (L. & C.)
35. State shortly the conditions of a valid contract for the sale of goods for future delivery ? (S. of A.)
36. Rule a form of Invoice, putting in whatever you please in the way of headings to make it look like a real Invoice, and enter the following—  
1 pc. × 27 Coating, 56 yds. at 4s. 2d. per yd.  
1 " 36 " 37 " at 3s. 9d. " " yd.  
1 " 0127 Trousering, 48 yds. at 3s. 3d. per yd.
- Terms : 1½%, one month. Deduct the discount and receipt the Invoice.  
(S. of A.)
37. You are an exporter of stationery, and have received an order from Melbourne for your stock lines, value, say, £100. State the procedure you would follow in getting the goods to your customer in Melbourne.  
(S. of A.)
38. A merchant may quote a price for goods f.a.s., which means that the price includes the cost of conveying the goods to the ship's side. Mention five other kinds of prices commonly quoted for goods, give their commercial abbreviations, and explain exactly what the prices mean.  
(S. of A.)
39. An importer of foreign goods has to "declare" the consignments he receives. What is meant by "declaring" goods and how is it done ? What is the procedure followed by an importer to obtain possession of dutiable goods ?  
(S. of A.)
40. What are the usual terms of purchase of goods by a retailer from a wholesale warehouse or a manufacturer ?  
(S. of A.)
41. It has been stated (a) that the modern tendency is towards retail business on a large scale, (b) that expenditure on organisation tends to increase rapidly with the size of the business. Can you reconcile these statements ?  
(S. of A.)
42. What is discount ? When and why is it given, and whom does it advantage ?  
(S. of A.)



43. State shortly the main differences between home and foreign wholesale trade. (S. of A.)

44. What is a Trade Discount? Mention four kinds of commodities usually sold subject to such a discount. (S. of A.)

45. What is a Tender, and what purposes does it serve? (S. of A.)

46. From the point of view of the wholesale export trader, what constitutes the satisfactory execution of an order by a manufacturer who has placed the goods f.o.b.? (S. of A.)

47. What are the advantages of a Departmental Stores—

(a) To the general public?

(b) To the trader, as distinguished from confining his capital and energies to a single trade? (S. of A.)

48. What are the distinctive features of Multiple Shops? (S. of A.)

49. How may foreign traders safeguard themselves against the risks of Exchange? (S. of A.)

50. Many manufacturers in the Midlands, and elsewhere, have London agents. What are the duties of these agents, and what purposes do they serve? (S. of A.)

51. What are Gross Profits? What is the object of ascertaining Gross Profits? (S. of A.)

52. Mention three commodities usually sold by standard, and three commodities usually sold by sample. Can you suggest any reason why some commodities are customarily sold by standard and others by sample? (S. of A.)

53. What functions are served by the Wholesaler in connection with food-stuffs? (S. of A.)

54. Do you consider Interest on Capital a part of Profit, or a charge against Profits? Give reasons for your answer. (S. of A.)

55. Define "Cheque." Draw a cheque for £80. What precautions should be taken in drawing the cheque to protect it in case of loss? (L. & C.)

56. What are the functions of banks? Show how the Banking system is of service to traders. (L. & C.)

57. What are the essentials of a Bill of Exchange? James Robinson sells William Brown goods to the value of £101. Robinson agrees to take Brown's acceptance. Draw the necessary bill, making it payable three months after date and accepted payable at Stuckey's Bank, and state what stamp it will require. (L. & C.)

58. What are the uses and advantages of Bills of Exchange? (L. & C.)

59. State and explain what arrangements were made by the Government in regard to the financial crisis consequent on the outbreak of the present war. (L. & C.)

60. What are the special uses and functions of—

(a) The Bank of England?

(b) The Bankers' Clearing House? (L. & C.)

61. What are the functions of money? (L. & C.)

62. What is the equivalent in £ s. d. of 1 oz. of standard gold; and what does standard gold consist of? (S. of A.)

63. Write explanatory notes on any five of the following: (a) Gentlemen's agreements; (b) mergers; (c) over-capitalisation of industry; (d) standardisation and elimination; (e) co-operative marketing; (f) co-partnership; (g) customs entries; (h) brokers. (N.U.T.)

64. How many kinds of Banks are there, and what are they, and how do they differ? (S. of A.)

65. Explain the meaning of the following items, and state where they should appear in the Balance Sheet of a Bank—

(a) Cash in Bank of England.

(b) Acceptances and Guarantees (as *per contra*).



- (c) Deposit Accounts.  
 (d) Rebate on Bills not due.  
 (e) Liabilities of Customers for Endorsements on Foreign Bills (as *per contra*).  
 (f) Interest due on Investments. (S. of A.)
66. Mr. John Brown, of Leeds, buys goods value £30 of Mr. James White, of Preston. He gives a three months' bill of exchange on 10th January. Draw the bill and show the acceptance. (L. & C.)
67. State the advantages of a Banking Account to a trader. How do you open such an account? (L. & C.)
68. Mention two advantages of the cheque system. Draw out a form of cheque on the Westminster Bank, Ltd., for £112 8s. 6d. in favour of Wm. Johnson & Son. Sign it "Fred Jones," and make it as safe a document as you know how. (L. & C.)
69. Explain the meaning of four of the following terms used on the Stock Exchange—  
 (a) Coupons (c) Jobber's turn (e) Options  
 (b) Consols (d) The carry over (f) Settlement (L. & C.)
70. What are the functions of credit? State concisely the disadvantages of credit. (L. & C.)
71. What are the functions and advantages of Banking? (L. & C.)
72. What is (a) a "bull point";  
 (b) a "bear point"?  
 What (if any) are the uses of "bulls" and "bears" to the community? (S. of A.)
73. What are "'futures' in cotton?" How are they worked? When are they legitimate business transactions, and when purely speculative transactions? (S. of A.)
74. What are "fluctuations in exchange," and what causes them? (S. of A.)
75. What is the Bank Rate? What causes it to fluctuate, and why is it usually higher in the Autumn? (S. of A.)
76. A Bank advances money upon goods shipped on consignment abroad. How would the Bank secure this advance in the ordinary way of business, and how would it proceed to collect the amount owing to it in due course? (S. of A.)
77. A owes £5 each to B, C, and D. In discharge of his indebtedness he forwards, by post, five Postal Orders of £1 each to B; a Money Order for £5 to C; and a crossed cheque, drawn on his bankers, to D. You are asked to state as clearly as you can how the actual payment is carried into effect in each case, including in your explanation all intermediate operations. (S. of A.)
78. What do you know about the Bankers' Clearing House? (S. of A.)
79. How, and to what extent, may credit be used as a substitute for metallic currency? (S. of A.)
80. How would you expect the Bank of England Weekly Return to be affected by the issue of a large Government Loan? (S. of A.)
81. Why is the market rate of discount often different from the Bank Rate? (S. of A.)
82. How, and why, does war affect Rates of Exchange? (S. of A.)
83. Write short notes on any *two* of the following: (a) The advantages of a bill of exchange to a creditor; (b) the various ways of remitting money through the post; (c) a good system of filing; (d) the qualities of an efficient salesman. (N.U.T.)
84. What is Par of Exchange? (S. of A.)
85. State the exact effect of crossing a cheque (a) generally, (b) specially. (S. of A.)



86. How does a Savings Bank (e.g. the Post Office Savings Bank) differ from an ordinary Bank? (S. of A.)

87. What is a Bank? Frame your answer so as to exclude concerns which, in your opinion, carry on business improperly under the name of a Bank. (S. of A.)

88. What is a Moratorium? What purposes does it serve, and what are its limitations? (S. of A.)

89. Why does commerce grow with an improvement of transport facilities? Mention some transport improvements that have aided the growth of commerce. (L. & C.)

90. Distinguish and explain—

(a) Mate's Receipt

(c) Charter Party (L & C.)

(b) Bill of Lading

91. Explain the following terms in a policy of Marine Insurance—

(a) Perils of the Sea

(d) Barratry

(b) Thieves

(e) All other perils (L. & C.)

(c) Jettisons

92. What is the object of insurance? Give illustrations from different kinds of insurance with which you are familiar. (L. & C.)

93. What considerations would guide you in deciding whether to send goods (a) by road, (b) by rail, (c) by canal? (S. of A.)

94. Write a short essay on the effect of the opening of the Panama Canal on British oversea trade. (S. of A.)

95. What effect have fluctuations in the cost of transit upon (a) prices, (b) the volume of trade? (S. of A.)

96. What is (a) a Charter Party? (b) a Bill of Lading? (S. of A.)

97. What are the usual conditions of a contract of Marine Insurance? (S. of A.)

98. How are Railway Rates determined in this country? (S. of A.)

99. In what way or ways is the wholesale warehouseman of service to the consumer? In what circumstances can the retailer make purchases direct from the manufacturer? Give illustrations. (L. & C.)

100. State shortly what are the relations of the Wholesale Warehouse to the retailer. Describe in what ways such a warehouse is of assistance to the retail trade. (L. & C.)

101. Describe briefly the organisation of any wholesale market that you are acquainted with. (L. & C.)

102. State shortly what Salesmanship consists of. (S. of A.)

103. In what ways may masters combine for common purposes? (S. of A.)

104. Into what divisions, for convenience, may commerce be divided? Show how the members in each of the divisions are interdependent. (N.U.T.)

105. What is meant by a "business undertaking"? Show the influence of the economic environment on the development of the business unit, quoting examples in illustration of your answer. (N.U.T.)

106. Why do some manufacturers dispense with the wholesaler and supply the retailer direct? How have they been able to do so? (N.U.T.)

107. Enumerate the chief factors which determine the localisation of industry. Illustrate your answer by reference to the location of industries in your own country. (N.U.T.)

108. Mention some finished article in which you are interested and trace it back to the source whence it came as a raw product, giving the various classes of labourers required before the article reaches the ultimate consumer. (N.U.T.)

109. "The modern tendency is to abolish the middleman." Discuss this statement from the point of view of the (a) manufacturer, (b) retail merchant, (c) consumer. (N.U.T.)



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